

USAID/CAUCASUS – GEORGIA COUNTRY STRATEGY

FY 2004 - 2008

---ABRIDGED VERSION---

This Strategic Plan for USAID/Caucasus -Georgia was assembled by the USAID/Caucasus-Tbilisi Mission. This Strategic Plan is a “pre-decisional” USAID document and does not reflect results of USG budgetary review. Additional information on the attached can be obtained from the Senior Program Information Officer, Program and Project Support Office, USAID/Caucasus-Tbilisi.

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USAID/CAUCASUS – GEORGIA

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Embassy of the United States of America

Tbilisi, Georgia

July 31, 2003

Mr. Kent Hill
Assistant Administrator
Europe & Eurasia Bureau
USAID
Washington, D.C., 20521

Subject: USAID/Caucasus-Georgia Country Strategy 2004-2008

Dear Mr. Hill:

I am pleased to endorse USAID/Caucasus-Georgia's Country Strategy 2004-2008. The US Mission/Georgia reviewed the draft and had an opportunity to provide comments and input. The final product reflects our joint effort. USAID Director Farbman presented the Country Strategy to the Framework Group of most active bilateral and multilateral donors, who were pleased with its breadth and focus.

The proposed Strategy builds on the experiences gained in implementing programs under the current Strategy (2000-2003), and also directly contributes to accomplishment of Mission Performance Plan (MPP) goals. The core Strategic Objectives dealing with economic growth, energy, democracy, and health and social development are no doubt the right priorities, given Georgian needs and our comparative advantage. The three Special Initiatives – elections assistance, anti-trafficking in persons, and anti-corruption – proposed in the Strategy are critical for the future of Georgia and are among the urgent concerns of U.S. foreign policy as I write this message.

The programmatic approach proposed by USAID/Caucasus-Georgia, which emphasizes working less with central governmental institutions and more with the private sector, NGOs and local governments in the regions, is a realistic one, given the constraints of working with the government at present. However, as the Government of Georgia (GoG) becomes a more serious development partner and responsive to critically needed reforms, it may be possible in the future to increase USAID's work with the GoG.

While we are endorsing the five-year Strategy as written, we also are aware of the impact the forthcoming Parliamentary elections in November 2003 and the Presidential elections in 2005 may have on implementation of the overall Strategy, especially if the elections are not held in a transparent way. We are cautiously optimistic about the positive outcome of the elections, but we are nevertheless protecting our options. Anti-corruption is another major issue affecting Georgia's development. I am pleased that reasonable levels of resources are dedicated to this effort in the Strategy. Anti-trafficking efforts are important too, both from the moral and human rights perspectives, not to mention the

special requirements that will need to be met by the GoG to pull itself out of "Tier 3" status.

All told, USAID has done an outstanding job in researching this strategy, consulting widely in the stakeholders community, and in presenting a compelling analysis as to how to advance the economic, democratic and social transitions in Georgia. All sections of Embassy/Tbilisi will work in coordination with the Mission to ensure we achieve the best results possible in this challenging and dynamic environment.

Sincerely,

A handwritten signature in cursive script, appearing to read "Richard Miles".

Richard Miles
Ambassador

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ACRONYMS

ABA	American Bar Association
AC	Anti-corruption
ACDI/VOCA	Agricultural Cooperative Development International/Volunteers in Overseas Cooperative Assistance
ADS	Automated Directives System
ADP	Automated Data Processing
AES	American Energy Systems of Virginia
BP	British Petroleum
BTC	Baku-Tbilisi-Ceyhan
C&R	Correspondence and Records office
CARE	Cooperative for American Relief Everywhere
CBED	Community-Based Economic Development
CBO	Community-Based Organizations
CCI	Cross-Cutting Issue
CEELI	Central European and Eurasian Law Initiative
CELD	Constituents Engaged in Local Decision-Making Project
CIP	Community Investment Program
COE	Council of Europe
CPI	Corruption Perceptions Index
CSO	Community Service organization
DG	Democracy and Governance Office
DOD	Department of Defense
DOT	Department of the Treasury
E&E	Europe and Eurasia Bureau
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EE	Energy and Environment Office
EF	Eurasia Foundation
EG	Economic Growth Office
ESAF	Enhanced Structural Adjustment Facility
EU	European Union
EWG	Energy Working Group
FDI	Foreign Direct Investment
FINCA	Foundation for International Community Assistance
FSN	Foreign Service National
FSU	Former Soviet Union
FY	Fiscal Year
GAI	Georgia Assistance Initiative
GCMi	Georgia Community Mobilization Initiative
GDA	Global Development Alliance
GDP	Gross Domestic Product
GEF	Global Environmental Facility
GEGI	Georgia Enterprise Growth Initiative
GMSE	Georgia Microfinance Stabilization and Enhancement

GNERC	Georgia National Electricity Regulatory Commission
GoG	Government of Georgia
GSE	Georgia Electricity Dispatching Company
GSIF	Georgia Social Investment Fund
GTZ	German Technical Assistance Agency
GWEM	Georgia Wholesale Electricity Market
GWHAP	Georgia Winter Heating Assistance Program
HIV/AIDS	Human Immunodeficiency Virus/Acquired Immunodeficiency Syndrome
HSD	Health and Social Development Office
ICASS	International Cooperative Administrative Support Services
IDA	International Development Association
IDP	Internally Displaced Person
IEC	Information Education Communication
IFC	International Finance Corporation
IFES	International Foundation for Electoral Systems
IFIs	International Financial Institutions
IG	Inspector General
ILO	International Labor Organization
IMF	International Monetary Fund
IOM	International Organization for Migration
IR	Intermediate Result
IREX	International Research and Exchange Board
IRI	International Republican Institute
IT	Information Technology
KfW	Kreditanstalt für Wiederaufbau (German organization)
kWh	kilowatt-hour
LGP	Local Guard Program
LGRI	Local Governance Reform Initiative
MCA	Millennium Challenge Account
MOLHS	Ministry of Labor, Health, and Social Protection
MPP	Mission Performance Plan
MW	Megawatt
NBFI	Non-Banking Financial Institution
NBG	National Bank of Georgia
NGO	Non-Governmental Organization
NIS	Newly Independent States
NOB	New Office Building
OE	Operating Expenses
OYB	Operational Year Budget
ORF	Oil Revenue Fund
PAS	Public Affairs Section
PD&S	Project Development & Support
PMP	Performance Monitoring Plan
PREGP	Poverty Reduction and Economic Growth Program
PVO	Private Voluntary Organization
RFA	Request for Application
RFP	Request for Proposal

RoL	Rule of Law
RWMP	Regional Water Management Program
SAVE	Support Added-Value Enterprises
SI	Strategic Initiative
SJ	Samtskhe-Javakheti region
SME	Small and Medium Enterprises
SO	Strategic Objective
SOE	State-Owned Enterprise
SP	Strategic Plan
START	Strategic Technical Assistance for Results with Training
TAAPE	Transparency, Accountability, Awareness, Prevention, and Enforcement
TB	Tuberculosis
TCN	Third Country National
TI	Transparency International
TIP	Trafficking in Persons
UDC	United Distribution Company
UNDP	United Nations Development Program
UNICEF	United Nations International Children and Education Fund
USDA	U.S. Department of Agriculture
USDH	U.S. Direct Hire
USG	United States Government
USPSC	U.S. Personal Services Contractor
VAT	Value Added Tax
WB	World Bank
WB MDF	World Bank Municipal Development Fund
WTO	World Trade Organization

I. INTRODUCTION AND STRATEGY

A. U.S. Foreign Policy Interests

Georgia's independence, sovereignty and viability are strategically important for the U.S. in our efforts to stabilize the volatile Caucasus/Central Asia region bounded by Russia, Iran and Turkey. Regional stability, democracy, economic prosperity and security, and counterterrorism are recognized in the U.S. Mission Performance Plan (MPP) as the primary interests served by USG policy towards Georgia. Georgia continues to maintain a policy of openness to the West, and actively seeks closer and stronger formal ties with the U.S. and Europe.

Regional stability is the first priority of U.S. foreign policy. Attempts by two autonomous regions, Abkhazia and South Ossetia, to secede from Georgia triggered a civil war, a flow of nearly 300,000 internally displaced persons (IDPs), and deterioration of law and order. Although the situation has somewhat stabilized since 1995, final political settlement of these internal conflicts has yet to be reached. These conflicts are compounded by the adjacent war in Chechnya and Chechen refugee flows from Russia. Meanwhile, Russian military bases remain on Georgian soil. USAID has played, and will continue to play, a pivotal role in fostering Georgia's transformation to a stable, market-oriented, democratic country.

Georgia's central role in the Eurasian east-west energy and transportation corridor is vital to the economic viability of the entire region and its integration with Western political, economic and security structures. With strong USG support and encouragement, international corporations have signed agreements with Georgia and other countries in the region for oil and gas transit through Georgia: the Baku-Tbilisi-Ceyhan and Shah Deniz oil and gas pipeline projects have just started construction.

B. Introduction to the Socioeconomic and Political Setting

Georgia faces a major political transition over the next three years second only in political magnitude to the challenges to regional stability. The final term of President Eduard Shevardnadze, Georgia's leader for the last ten years, will expire in 2005. Georgia already is gearing up for the 2005 Presidential elections, with Parliamentary elections due in 2003 as a major indicator of what will happen. Georgia, however, is beset by challenges to a stable, democratic transition. The corrosive effects of the war in neighboring Chechnya and the lack of responsible governance in the breakaway autonomous regions have made Georgia vulnerable to organized crime, trafficking, and international terrorism. The delicately balanced Western-oriented coalition which has governed Georgia is fragmenting, leaving democratic forces weakened relative to forces representing the rent-seeking elites. Corruption has harshly impacted a voting population disenchanted with Western-style democracy. Georgia's economic crisis is the next large problem facing the country. The crisis is caused by difficulties in collecting revenues, improper budgeting of expenditures, a persistent energy shortage and a deteriorating business and investment climate. All of these components have corruption as well as poor management and organization as their root cause. Wages and pensions are low and often months in arrears, and state support for the education and health care systems has all but collapsed. Economic stagnation jeopardizes the

long-term viability and prosperity of Georgia as an independent, democratic, market-oriented nation.

Georgia's internal weakness means that unless corrections are made soon, the prospects for a democratic and prosperous sovereign Georgia, able to withstand Russian pressure, could be at risk. Georgian government unwillingness or inability to implement serious reforms in key sectors draws into question an assistance strategy predicated on GoG commitment to democratic change, economic growth, and social justice.

U.S. policy over the next three years, geared by the two upcoming elections, will focus its priorities on these challenges: creating a stable environment for democratic elections, stimulating an economy that will win the allegiance of the electorate to market and democratic reform, and helping the electoral process.

C. Economy and Private Enterprise

The Georgian economy experienced a catastrophic decline after the break-up of the Soviet Union -- an estimated 60 percent drop from 1989 Soviet republic levels. Growth in GDP, for example, has been volatile, rising from an abysmal minus 11.4 percent in 1994 to 10.8 percent in 1997. This growth has been skewed to a handful of sectors (*e.g.*, communications, transportation, and finance) and is of doubtful sustainability over the longer term.

The relative stability of the lari, which Georgia introduced in the mid-1990s, continues to be one of the government's major economic successes. In the mid-1990s the government also tamed inflation, carried out large-scale privatization, and enacted fairly liberal economic legislation. Georgia has no currency controls, is only the second country in the former Soviet Union to join the WTO, and has completed substantial land privatization. Through USAID assistance, 2.4 million -- mostly small -- parcels have been surveyed, registered, and titled to their legal owners.

Meanwhile, fundamental economic problems have eroded external and internal investor confidence. After 1999, however, both political and economic reforms slowed. Since 1994, Georgia has largely followed the World Bank and the International Monetary Fund's recommendations for macroeconomic policies. While the reformist camp of the leadership generally supports economic liberalization and considers the Bretton Woods institutions, USAID, and other Western institutions to be its allies in this process, many other government officials resist carrying out reforms. Extortion by various government agencies and the existence of "chosen" economic agents that enjoy significant privileges distort economic competition. For example, in the early 1990s, officials who were opposed to reform exempted from privatization most large manufacturing enterprises on the grounds that they were strategic national assets. It is much more difficult to privatize these companies now, as their assets were plundered and they amassed huge debts.

The government's enduring inability to collect taxes has led to a severe, ongoing fiscal crisis that began in 1998. The 2001 budget was cut by one-fourth in the fall but even this reduced target was missed by 87 million lari (\$43 million). The United Nations Development Programme (UNDP) puts the figure for the "shadow" economy at 70 percent. For example, 75 percent of small and medium size enterprise (SME) turnover, 60 percent of the tobacco

business, and 70 percent of fuel imports go officially unreported.

Despite the country's fiscal crisis, the National Bank of Georgia (NBG), the central bank, operates with professionalism and integrity. Public confidence in banking institutions has been increasing; between 1996 and 2003, commercial bank deposits increased seven-fold. However, the absolute volume of deposits is still low and major banks do most of their business servicing government spending and international credits. High interest rates, up to 3 percent per month, make lending problematic.¹

Foreign direct investment (FDI) has been volatile in recent years. According to the Georgian State Department of Statistics, FDI was \$145.8 million in 2002, \$109.9 million in 2001, \$131.2 million in 2000, compared to \$83.65 million in 1999. FDI peaked in 1998 at \$288 million, although a significant portion of this is attributable to one project: the completion of the Baku-Supsa early oil pipeline and Supsa terminal. The United States is the largest foreign investor in Georgia. U.S. companies have invested \$52.7 million since 1999, or between 20 - 30 percent of overall FDI each year. However, the unhappy experience of AES, the largest U.S. investor in Georgia, certainly will further darken the chances of significant FDI in the foreseeable future.

The government largely completed price liberalization by 1996, with energy and urban electric transport the only areas where prices remained controlled. Perhaps not coincidentally, severe energy shortages and price distortions have become a symbol of the Georgian economic crisis. Early after independence, Tbilisi typically enjoyed only four to six hours of electricity per day in winter, while most of the rest of the country averaged three to four hours and some areas even less. The 1997 Electricity Law called for establishing the independent Georgian National Electricity Regulatory Commission (GNERC), the creation of which USAID actively urged and directly supported. GNERC adopted a transparent tariff framework and issued licenses to sector enterprises. A wholesale electricity market (WEM) was created, with major power distributing and generating companies consolidated and privatized, including the critical Tbilisi market under AES/Telasi.² In a "two-steps-forward, one-step-back" sort of process, GNERC's supposedly independent rate decisions have been overruled by Georgia's Constitutional Court. As a result, most electricity distribution entities remain financially unsustainable, and non-payment for electricity usage is the norm. The government has begun extending the same regulatory approach to the natural gas sector with similar results. Georgia currently imports its gas from Russia, and purchases electricity in the winter from Russia and Armenia. Since gas is crucial for domestic electricity generation and heating, Russia's monopoly of gas supplies constitutes a major problem given the strained relations between the two countries.

The agricultural sector is likely to remain Georgia's bedrock for sustainable growth. Georgia has a multitude of microclimates and rainfall patterns that provide the diversity necessary to enable production of a broad range of agricultural commodities. During the Soviet period, it was one of the primary "internal market" suppliers of fresh fruits and vegetables, as well as a variety of processed agricultural products such as wine, juices and jams. In the continuing aftermath of the Soviet command economy, there are currently very few organized domestic

¹ US\$ 3-month commercial paper rate, 3.13 percent for 2003 (estimated): The Economist Intelligence Unit.

² Owned by American Energy Systems of Virginia.

or export marketing channels for agricultural products and, therefore, limited demand for those products. Without demand, there is no compelling reason for producers or processors to invest in improvements, inputs, management or processing technology. Foreign and domestic investment, bank loans, joint venture partnerships, and other financing remain limited. However, without these improvements, Georgia will not be competitive on world markets. In short, Georgia is trapped in a downward cycle of declining market demand, production and processing.

D. Social Transformation

Georgia's enduring fiscal crisis exacerbates social problems and undermines the government's ability to address major problems facing the country. Unemployment stands at 24 percent, with 38 percent economically inactive, both of which figures have been growing since 1996. The difficulty of finding work, given the dramatic drop in economic production since independence, has forced many Georgians to look for alternatives to formal jobs, leading to an increase in the number of self-employed workers. More than 78 percent of self-employed workers are engaged in agricultural activities that allow them to avoid hunger but provide small -- if any -- monetary incomes. Land, family networks, entrepreneurial spirit, and remittance income have become the principal tools for survival for the great majority of the Georgian people. For many public sector workers, the problem is underemployment; that is, limited employment at low remuneration. Unemployment has hit the most educated sectors of Georgian society; its levels are significantly higher in Tbilisi where about 30 percent of the economically active population is unemployed.

All female citizens over age 60 and male citizens over age 65 are entitled to pensions. The rate of pensions is universal (about \$6.50/month equivalent). Notwithstanding this paltry nominal entitlement, the state accumulated huge arrearages to pensioners. Forty-two percent of payments were in arrears in 1998 and 21 percent in 1999 because of Georgia's severe fiscal crisis and rampant corruption. USAID's Georgia Winter Heating Assistance Program (GWHAP) has mitigated some impacts on this vulnerable group, at least in urban areas where informal support systems are limited.

A special category of social instability results from the estimated 260,000 internally displaced persons (IDPs) from Abkhazia and Tskhinvali (South Ossetia), who have little hope of returning to their homes and communities and who strain Georgia's already-overstretched social services infrastructure. U.S. assistance programs in Georgia aim to reduce IDP suffering by helping to meet basic needs of vulnerable populations, while emphasizing local self-reliance and conflict resolution activities.

Georgia is both a source country and a transit country for trafficking -- mostly women working in the commercial sex/entertainment industry, as in Turkey, where reportedly 70 percent of arrested prostitutes in 1999 were of Georgian nationality. Trafficked Armenians destined for Turkey and Dubai also transit through Georgia -- perhaps 500-700 annually. While the GoG voices its commitment to combating trafficking, it lacks concrete action; corruption and a difficult economy are perceived as more high profile and immediate problems.

The current level of education in Georgia is on a par with that in high-income countries.

Public funding for education, however, has been shrinking. In 1999, Georgia spent 2.2 percent of GDP on education, compared to about 5.4 percent in Eastern European countries and 3.7 percent in Latin America. Georgian primary schools have a 95 percent graduation rate. Of those who graduate, 97 percent enter Level I secondary schools; approximately 96 percent of these students graduate. However, only 59 percent of Level I graduates continue to Level II secondary schools. As would be expected, the disparities are worse in the rural areas. Under-the-table tuition payments pervade the system, becoming more demanding in the upper echelons. The schools remain probably the most important change agent for modifying values and attitudes, sometimes characterized in Georgia as a potent mixture of entitlement, resignation, and rent-seeking.

The infant mortality rate has more than doubled since 1993, rising from 20 to 43 deaths per 1,000 live births in 2000. Maternal mortality increased from 45 to 51 deaths per 100,000 live births. The primary health care system has broken down, and new approaches to management and funding are essential.

E. Civil Society and Governance

The successes and failures of democracy-building in Georgia are closely linked to the state-building process. The latter was challenged in the early 1990s by violent ethno-political and civil conflicts and continues to be seriously impeded by several factors. These include the existence of “frozen” conflict areas such as Abkhazia and South Ossetia; the uncertain status of the Autonomous Republic of Ajara; the ineffectiveness of state institutions; rampant official corruption; and spillover effects from conflicts elsewhere in the region, such as in Chechnya. A one-day military mutiny in May 2001 and an episode of renewed fighting in autumn 2001 in Kodori Gorge of Abkhazia, pitting Georgian and Chechen fighters against the Abkhaz militia, underscore Georgia’s volatility.

The process of democratic development in Georgia is uneven. The country has made considerable progress regarding the free operation of political parties, civic organizations, and the media, as well as in privatization and other areas of economic liberalization. This, however, has not led to the creation of an effective democratic system of governance, and the government has not put in place a framework for fair political and economic competition. The so-called “power ministries” and the law enforcement system resist reform (save for certain changes in the judiciary) and play a disproportionate role in the political process.

For the most part, there are no serious barriers to the formation and activities of political parties, except in Ajara. Although minority regions tend to have high turnout figures, ethnic minorities tend to support government-backed candidates and play a largely passive role in political life. Insufficient knowledge of the Georgian language, as well as a fear that their ethnicity may become an issue in political fights, are among the reasons that minorities do not get more involved in politics. Overall, the fairness of the election process is continually and widely questioned; whether the upcoming 2003 Parliamentary and 2005 Presidential elections will be fraud-free is an open question. Through IRI and NDI programs, USAID has taken the lead in helping Georgia’s Parliamentary voting blocs mature into issues-based, constituency-oriented parties, a work still in progress.

USAID assistance has been instrumental in developing surprisingly vital civil society NGOs in Tbilisi and throughout the country that effectively advocate members' rights and agitate for political and economic reform. This trend has been accelerated and strengthened by community development efforts. Nevertheless, the number of Georgians involved in NGOs remains only a small segment of society. A number of NGOs act as pressure groups -- such as by blocking or promoting certain legislation -- on a variety of issues, in a sense compensating for the weakness of the political opposition. For example, Section 3 of the Administrative Code, which is the equivalent of the Freedom of Information Act in the United States, was enacted mainly due to the activism of NGOs and journalists. Most NGOs, however, try to distance themselves from political parties. A negative side of the growing influence of NGOs is the proliferation of quasi-NGOs created by government agencies or political groups. Media outlets that are generally critical of Western values and influence often denounce NGOs in general as agents of such influence. The more pro-democratic media are largely sympathetic to NGOs and use them as their main source for expert opinions. Most NGOs are based around small groups of younger, more educated activists and, with few exceptions, have no real organizational structure.

Georgia's media are free from censorship. However, the government maintains control over some strategic outlets. Most independent media outlets lack professionalism, credibility, and financial viability, therefore making them vulnerable to influence through financial pressure.

Television is the main source of information for the vast majority of the population. Both national channels are state-controlled and give preference to official points of view, but appear now to be more balanced to compete with the Rustavi-2 independent channel. Rustavi-2 is the clear leader in terms of ratings, share of the national advertisement market, and influence on public opinion. Despite some allegations of bias, it tries to maintain balance in its political coverage.

All print media are formally private. However, the successors to erstwhile Communist newspapers, including the Georgian-language *Sakartvelos Respublika*, and its Russian-, Armenian- and Azerbaijani-language counterparts, receive government subsidies, have editors appointed by the President, and serve as official propaganda outlets. A proliferation of investigative reporting that alleges corruption or other crimes by high-ranking officials has led to an increase in the number of cases filed against journalists and media outlets. There are a number of journalists' associations and NGOs that promote media issues, and a major new USAID activity is working to strengthen these groups.

F. Quality of the Partnership

USAID Georgia's programs are by and large implemented by U.S. institutions (private firms and international PVOs), Georgian NGOs, and private sector institutions. These partners have proved responsive and have largely met their commitments. Under the current strategy, direct assistance to Government of Georgia (GoG) institutions has been limited and has been managed by U.S. contractors.

Georgia's relationship with donors has been cordial. However, GoG's development partnership in general has been less than satisfactory. Its commitment to economic reforms has been uneven, lacking in political will to implement reforms. While the GoG has

demonstrated its willingness to undertake policy and regulatory reforms and even passed several pieces of important legislation, implementation has been severely lagging, constrained by political interference and bureaucratic inertia. Reforms initially accepted and approved for implementation by one agency of the GoG often are contested by other agencies.

The unsatisfactory nature of Georgia's economic management by the GoG over the years resulting in heavy tax evasion, smuggling, and pervasive corruption have resulted in a huge annual loss of government revenues estimated as high as 35 percent of the national budget. This has created severe budgetary problems in meeting IMF and World Bank loan and credit conditionality. GoG's external debt has been rescheduled several times in the past years. However, this year for the first time Georgia has not been invited back to Paris Club negotiations. Inability of the GoG to fulfill its counterpart obligations to fund local staff and operating costs resulted in the EU's withdrawal of grants to the Ministry of Agriculture in 2002.

Recent developments in the energy sector -- such as the Parliament's apparently election-inspired move to impose deeply subsidized electricity rates -- have been disappointing. Inconsistent energy policies cannot but have a negative effect on further privatization of this key sector. The overall result of Georgia's poor economic governance, its inability to honor its commitments to donors, and poor record of implementation of reforms has created an environment not conducive to domestic or foreign direct investment.

Although the GoG has been a less-than-satisfactory partner at the national level, a growing number of local government institutions in the regions outside Tbilisi have been responsive and cooperative in implementing reforms/changes aimed at improving local governance, transparency in managing budgets, ensuring information flow to the population, and increasing local participation.

Notwithstanding its inadequacies in internal management, at the geo-political and strategic levels Georgia has been a dependable partner and ally in sharing and supporting U.S foreign policy goals, especially as they relate to immediate mutual interests in regional stability. This commitment has been evident in the GoG's promotion of the east-west energy corridor, its fight against terrorism, and its goal of joining NATO.

G. New Program Directions and Emphases: An Overview

More than a decade since the breakup of the former Soviet Union and Georgia's claiming independence for itself, the underpinnings of successful statehood remain problematic. Assumptions made on both sides -- Georgian and American -- that the transition to a market-based economy and democratic values could be made in timeframes analogous to the rate of progress in Central Europe have proven overly optimistic. Georgia in many ways is more evocative of a "developmental" state rather than a "transitional" one, with the need for fundamental institutions to be built (or rebuilt) from the ground up. The realization that Western economic/political models cannot necessarily be grafted onto Georgian organs of economy and governance has resulted in a strategic, and tactical, reappraisal of at least some assumptions.

With U.S. and other donor assistance, Georgia made impressive strides in the mid- to late-nineties -- in the aftermath of the civil war -- in establishing the legal, and to some extent the regulatory and administrative, framework for economic growth and democratic pluralism. But the forward momentum of reform has noticeably slowed as reactionary forces have reasserted themselves. The “shortcut” of top-down regeneration from Tbilisi now does not seem as tactically viable as a more sustained, grassroots effort – over commensurately longer timeframes -- based on community consciousness and community action.

Greater emphasis, even reliance, on grassroots action also seems necessary to combat a defeatist mindset amongst many Georgian citizens. Georgians seem to be acutely aware of how far down the ladder of social and economic indicators their country has slipped since independence in 1990. Forward-thinking Georgians want to rebuild and even surpass the old Soviet standard of living, but on new sustainable foundations, from the bottom up.

It is USAID/Caucasus’ sense that this commitment at the grassroots must be formed from a new set of values and attitudes that replaces a culture of entitlement with a culture of responsibility, and a culture of “rent-seeking” with a culture of “lawfulness.”³

The existing (FYs 1999-2003) Georgia Country Strategy had already placed emphasis on community-based programs, and much of the needed interventions are now active or soon will be in each of our Strategic Objectives.⁴ NGO and local government development, the “value-added” agribusiness activity, scaled-down electricity distribution systems under the Energy Security Initiative, and the Georgia Community Mobilization Initiative (GCMi), for example, all have demand-driven, bottom-up operational styles at the core of their respective approaches. The new Country Strategy would take these grassroots initiatives to the next level of cohesion by explicitly coordinating more of this activity at the local or operational level for maximum total effectiveness. It is impractical and inappropriate for all USAID community-based interventions to be subject to more formal coordination, since some stand-alone efforts are of high value in the larger Georgian socio-economic context. However, more of our program has been scrutinized to see how it fits within a synergistic framework that has a greater likelihood of having significant impact at the local level on the issues of values, attitudes, and mindset as well as on the more traditional USAID objectives of social transformation, economic growth, and democratic pluralism.

Strains at the national and local level also suggest that the Mission adopt a strategy, and programmatic techniques, that explicitly seek to prevent conflict. Whether conflict arises out of ethnic, religious, or linguistic origins, its effects potentially threaten the very viability of the Georgian nation.

While our new strategy may have shifted even more sharply to people-level and community-level impact, USAID is not backing away from engagement with the GoG. Policy change in national institutions is still essential to long-term success. We expect that creating a greater voice and competence in local communities will drive a policy reform agenda through elected officials, business and professional groups, and the civil society at large. This

³ Acknowledgement to Dr. Roy Godson, A Guide to Developing the Culture of Lawfulness.

⁴ “Community” in this context is defined as the interactions of people of common interests in a common location, or sharing economic, ethnic or otherwise identifiable characteristics within a larger society.

approach could be especially important in the run-up to the 2003 Parliamentary and 2005 Presidential elections, where political posturing may dominate dialogue at the national level. Positive electoral outcomes would create the environment to resurrect reform proposals. Conversely, missed opportunities in these elections need not sidetrack the building of local institutions bettering Georgian citizens' lives. USAID must be ready to move, either way.

II. STRATEGIC OVERVIEW

This section references the Parameters Memorandum (Annex A) given the Mission by the Europe & Eurasia Bureau to guide development of the new Country Strategy, the goal and sub-goal the Mission has chosen; and Cross-Cutting Issues (CCIs) and Special Initiatives (SIs) that both highlight and impact our strategic thinking. Linkages to Agency policy and programs considered in development of the Country Strategy also are discussed.

A. Strategic Goal and Sub-Goal

The strategic goal is to **strengthen communities' capacity to rebuild essential services, restore income, and empower all citizens of Georgia to have an effective voice in government.** This goal is accompanied by a sub-goal of almost parallel importance to **foster new values and attitudes that encourage citizens of Georgia to be responsible and accountable for the direction of their country.** USAID/Caucasus-Georgia believes that the new Country Strategy can make a meaningful contribution towards achievement of these goals within the five-year timeframe, recognizing, of course, that renewal and adoption of new attitudes and behaviors is generational in scope.

At the goal level, there are three indicators of achievement: (1) per capita incomes increase in real terms; (2) public expenditures as percent of GDP increase for health and education; and (3) an increase in the World Bank Institute/Stanford University "voice and accountability" indicator used in the Millennium Challenge Account (MCA) country scores. (This last indicator is also known as the "KKZ" indicator.) At the sub-goal level, the indicator will be the KKZ "corruption" indicator, which is a composite of leading corruption indicators and is also used in the MCA ranking system. See Annex R for details concerning the MCA indicator system.

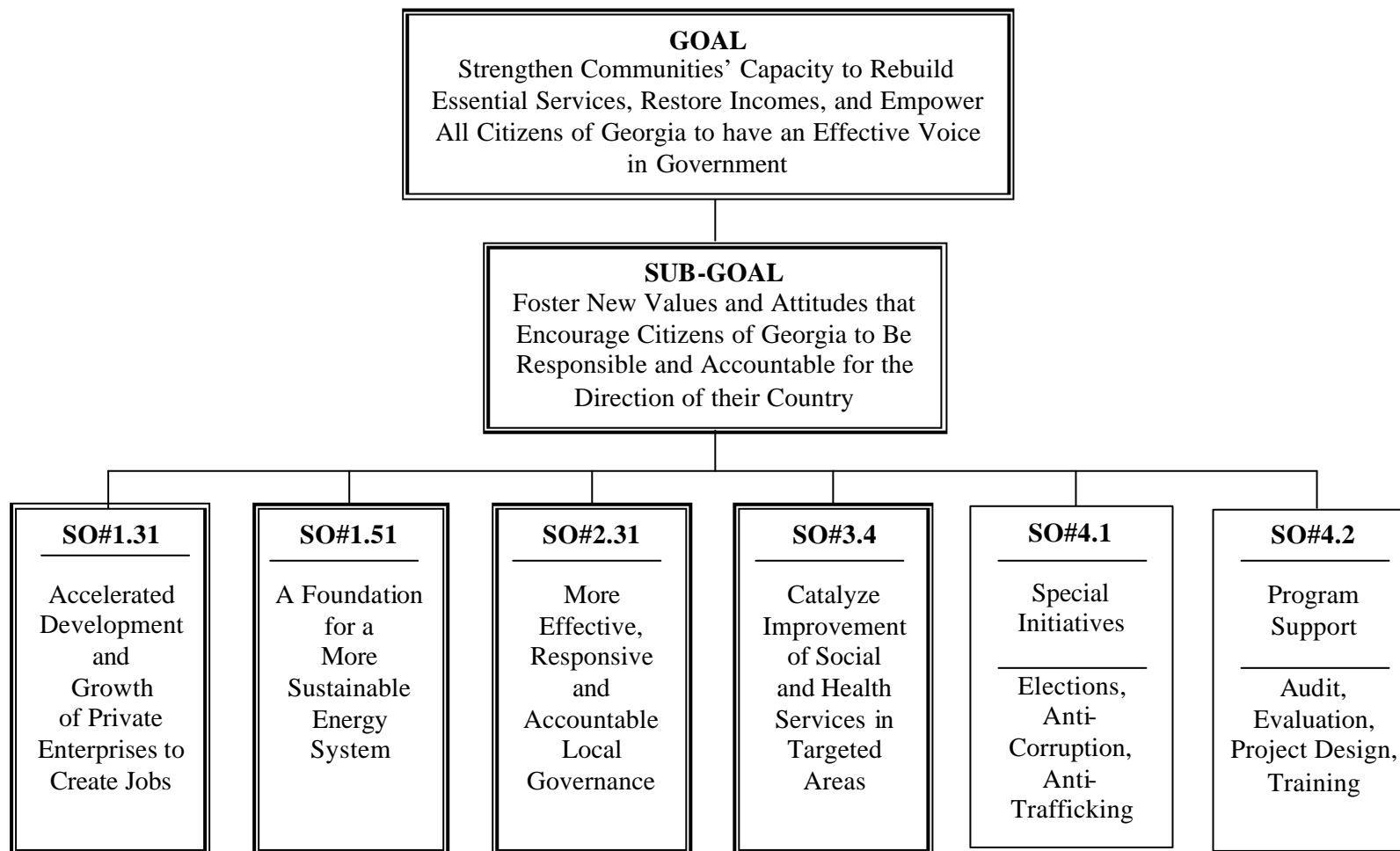
The new goal and sub-goal statements are evolutionary and represent a continuation from the FY 2000-2003 strategy's process of shifting program emphasis from establishing the macro-level enabling environment to "increased attention on impact at the local and individual level." Today there is even greater consensus among development professionals that, for the moment, enabling environment interventions at the national level may have diminished utility unless and until communities' economic underpinnings, shared responsibility for the restoration of key services, and political empowerment are strengthened. National level policy and institutional reform will remain tools of the USAID program, but more of the agitation for change will be from, and through, local institutions, based on an agenda of perceived priorities at the community level.

The National Security Strategy of the USG, issued by the President in September, 2002, enunciates seven developmental principles that clearly apply to U.S. assistance host countries in general and Georgia in particular:

- pro-growth legal and regulatory policies to encourage business investment, innovation, and entrepreneurial activity;
- tax policies – particularly lower marginal tax rates – that improve incentives for work and investment;

- rule of law and intolerance of corruption so that people are confident that they will be able to enjoy the fruits of their economic endeavors;
- strong financial systems that allow capital to be put to its most efficient use;

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- sound fiscal policies to support business activity;
- investments in health and education that improve the well-being and skills of the labor force and population as a whole; and
- free trade that provides new avenues for growth and fosters the diffusion of technologies and ideas that increase productivity and opportunity.

The new Country Strategy abides by these principles. The U.S. assistance program in Georgia, including Departments of Justice and Treasury activities, has active program goals in virtually all of these areas.

Strategic Framework Linkages

Economic Growth to Create Jobs

Mission SO 1.31 is supported by the MPP's Economic Growth and Development objective. SO 1.31 links directly with the Europe and Eurasia Bureau Objective (E&EO) 1.3 to accelerate development and growth of private enterprises which, in turn, links to the Agency Goal 1 to encourage broad-based economic growth and agricultural development.

Three Intermediate Results (IRs) are expected from SO 1.31: improved policy and operating environment; increased access to financial services; and increased market-driven production and sales.

Sustainable Energy System

Mission SO 1.51 also supports the MPP's Economic Growth and Development objective. SO 1.51 links directly to E&E's objective of a more economically sound and environmentally sustainable energy system which, in turn, links with Agency Goal 5 of "the world's environment protected for long-term sustainability."

Mission SO 1.51 posits three IRs: improved financial and commercial performance of energy sector entities; a more diversified, renewable and cost effective energy supply; and increased environmentally sustainable energy efficiency.

Accountable Local Governance

Mission SO 2.31 supports the MPP's Democratic Systems and Practices objective. SO 2.31 echoes verbatim E&E's objective of a more effective, responsive and accountable local governance which links to the Agency Goal of "democracy and good governance strengthened."

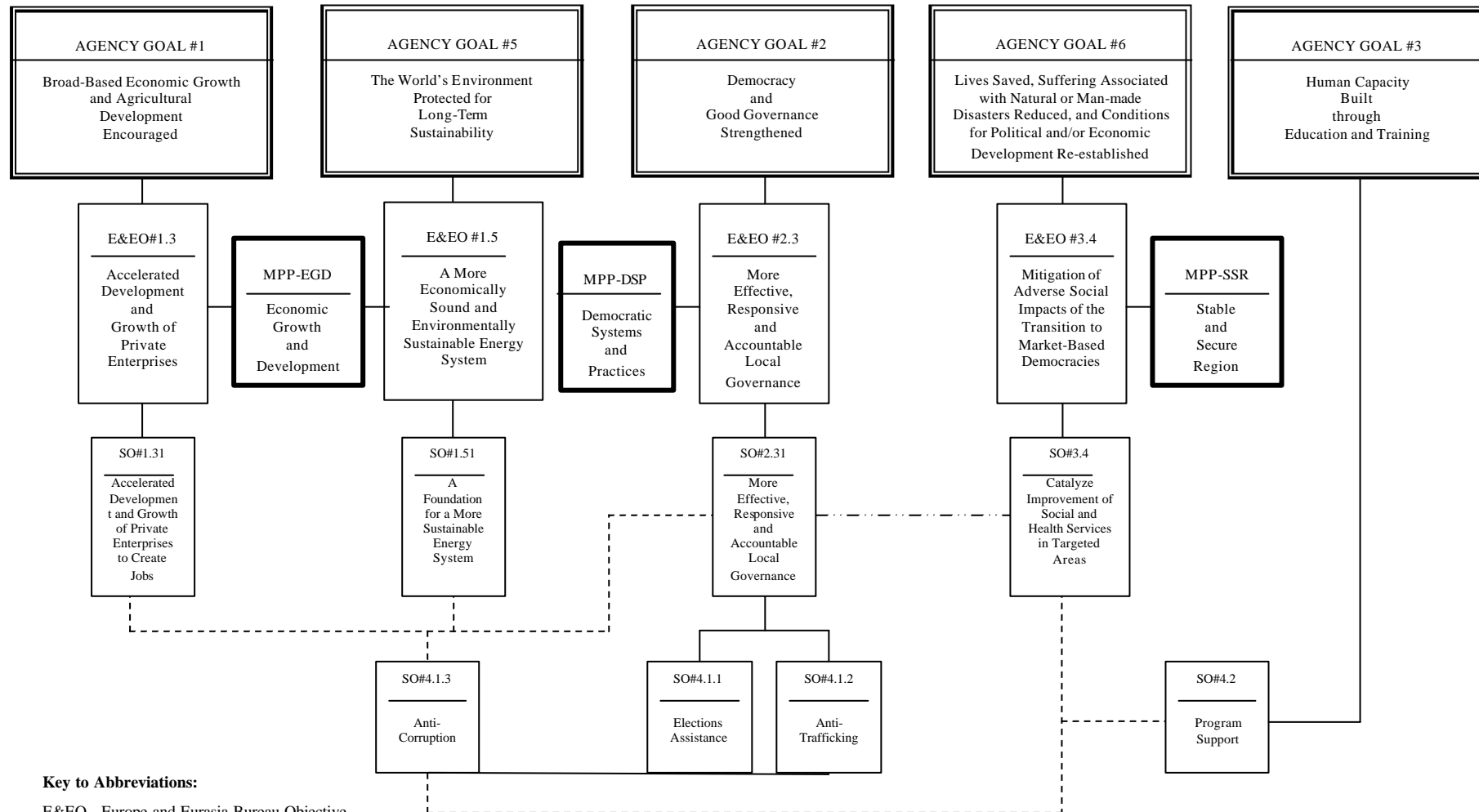
Mission SO 2.31 posits three IRs: independent media highlights citizens' concerns and informs communities of key issues; citizens' legal rights better protected; and improved capacity of local communities to engage local government.

Improved Social and Health Services in Targeted Areas

Mission SO 3.4 supports the MPP's Stable and Secure Region objective. SO 3.4's objective to catalyze improvement of social and health services in targeted areas links directly to E&E's objective – "mitigation of adverse social impacts of the transition to market-based democracies." In turn, E&E's objective supports the Agency Goal 6: "lives saved, suffering associated with natural or man-made disasters reduced, and conditions for political and/or economic development re-established."

USAID/CAUCASUS-GEORGIA COUNTRY STRATEGY OVERVIEW

LINKAGES TO AGENCY, BUREAU AND STATE DEPARTMENT STRATEGIC PLANNING DOCUMENTS



Mission SO 3.4 has two IRs: communities meet basic needs and prevention of disease; and access to quality health care improved.

The associated chart shows that SO 2.31 and SO 3.4 share certain developmental and managerial characteristics.

Special Initiatives

Mission SO 4.1 is comprised of three Special Initiatives: elections assistance, anti-trafficking in persons, and anti-corruption. The Mission's Office of Democracy and Governance manages the elections assistance Special Initiative. The trafficking in persons Special Initiative is co-managed by the Office of Democracy and Governance with the Missions' Program and Project Support (PPS) Office. The Regional Legal Advisor's office manages the anti-corruption Special Initiative as supported by five anti-corruption team members -- one from each of the four "core" Strategic Objectives and PPS.

Program Support

SO 4.2 supports all Mission activities with evaluation and audit services, training, and small grants and is managed in the Mission's Program and Project Support Office. SO 4.2 links directly to Agency Goal 3, "human capacity built through education and training."

With regard to the Sub-Goal statement, the USAID/Caucasus-Georgia Mission staff often raise the all pervasive issue of **values** and **attitudes** that hinder development in Georgia. Lack of jobs has led to serious out-migration and reinforces apathy among unemployed youth. An anachronistic attitude of "entitlement" among electricity consumers thwarts the normal interplay of market supply-and-demand forces. Soviet-era municipal administration stymies the natural give-and-take at town meetings. The contraction of health services and diminished educational outlays invite petty corruption. A substantial portion of these problems are attitudinal in nature and adversely affect values, trust, and social behavior. As a result, Georgians are a traumatized people. The Mission's four "core" SOs are logically linked to the Sub-Goal statement in that their successful implementation will underscore the benefits of self-regulating business associations, the critical social importance of paying one's debts, the added-value derived from listening to constituents, and the government's responsibility to regulate and monitor basic social services. If our SOs are successful in transforming relationships and expectations among citizens, then citizens will be sufficiently responsible and accountable so that they can begin to rebuild services, restore incomes, and enjoy an effective voice in government.

USAID/Caucasus believes its Country Strategy should extend through five fiscal years (FY 2004 to 2008) in order to establish and/or extend pilot programs in the economic, political and social spheres, to ramp up successful interventions, and to allow the benefits of planned program synergies to emerge. We believe that the transition to a more community-driven program should begin immediately, although we acknowledge that the outcomes of the 2003 and 2005 elections could have an impact on program mix and methodologies. Clearly, positive electoral outcomes could lead to a reversal of disengagement at the national government level, and even some redirection of program resources. The uncertainty of those outcomes, however, argues that USAID's core program not be dependent upon them. With or without optimum electoral results, the

predictability of the Georgian political/economic context is stable enough to support the notion that a five-year timeframe for the Country Strategy is sensible.

B. Cross-Cutting Issues, Special Initiatives, and Linkages to Agency Policy/Programs

The two Cross-Cutting Issues (CCIs) of **conflict prevention** and **youth** are long-term commitments which all four “core” SOs will address. Consistent with ADS 201.3.7.9, the Mission has three Special Initiatives: **Elections Assistance** which is fixed in time, **Anti-Trafficking in Persons** which is a U.S. foreign policy interest, and **Anti-Corruption** which, for this Mission, is exploratory in nature. Each initiative has its own stand-alone line item. None were deemed sufficiently complex to warrant an independent SO “status”. For this reason, the three Special Initiatives are aggregated under SO 4.1 while the two CCIs are shared by all four “core” SOs. (The new proposed activities are *intentionally* highlighted first in this section then further elaborated in Part III.)

In the analysis leading up to the formulation of the new Country Strategy, the Mission worked closely with its partners in frank and broad-ranging discussions and identified critical concerns common to many aspects of the present situation in Georgia. Some concerns, such as the commitment to help create sustainable jobs, fell clearly within the orbit of a specific SO and are presented in that context. Other concerns, such as the need to prevent conflict and help youth were Cross-Cutting Issues common to all four SOs. Lastly, three major concerns -- Elections Assistance, Anti-Trafficking in Persons, and Anti-Corruption -- presented unique and/or time-limited programmatic imperatives and are therefore treated separately as Special Initiatives outside the “core” SO structure.

Reflective of the above dialogue, the new Country Strategy presents six Strategic Objectives or SOs: four “core” SOs, a fifth SO comprised of three Special Initiatives, and a sixth SO covering normal program support.

1. Cross-Cutting Issues

a. Conflict Prevention

Problem: As a “new” nation reborn out of the collapse of the former Soviet Union, Georgia is exceptionally beset with nation-building challenges. None is more threatening to the very integrity of the modern Georgian nation-state than communal conflict among clans, regions, and the multiplicity of ethnic and religious groups that make up the fabric of the society. Parallel to these conflicts are the tensions inherent in a quickening democratic political process, with reactionary and reformist forces moving towards expected show-downs in the parliamentary election of 2003 and the Presidential election of 2005.

The origins of these conflicts are well known and were well outlined in the conflict vulnerability analysis done for the Mission, summarized in Annex B.⁵ The Caucasus region has been a cauldron of ethnic tensions since well before the Soviet, and even the tsarist, eras. At their worst, these tensions have found their current-day expression in the Abkhazia and Tskhinvali (South Ossetia) separatist movements, which threaten the territorial integrity of the country. Tensions continue to bubble in other regions of

⁵ Georgia Conflict Assessment. ARD, Inc. January, 2002.

Georgia, and may well be exacerbated by political posturing and appeals to various forms of “nationalism” in the run-up to the elections.

For the first decade of USAID’s program in Georgia, the strategic and operational impact of these conflicts was not, or at least did not appear to be, central to the success or failure of our transition programs, as USAID and the GoG struggled to put in place basic reforms and institutional capacities at the national level. (The clear exception to this was the Mission’s humanitarian assistance program, which early on had to cope with the after-effects of communal conflict and devise community-based programs to mitigate that conflict.) Increasing doubt about the GoG’s commitment to and capacity for national policy and institutional reform arose during the course of the 1999-2003 Strategy, and our program moved progressively toward an emphasis on grassroots, community-based development and building a strong base for political pluralism. The new 2004-2008 Country Strategy completes that journey.

Proposed Strategy: USAID will address conflict prevention at the regional, national and local levels in SOs 2.31 and 3.4. First, the program will promote conflict prevention strategies that ensure vigorous public debate but always in a peaceful, non-violent environment both pre- and post-elections. Second, SO Teams engaged in the design of conflict mitigation activities will be trained in conflict resolution skills, and the conflict mitigation dimension will be an explicit factor when designing those activities, program-wide. This will be a perfect complement to the Mission’s renewed emphasis on participatory, community-engagement and stewardship techniques. The Mission is already using these techniques, as in the Youth Houses and youth-led NGOs that apply psychosocial conflict prevention techniques to bring ethnic youth together in positive circumstances in separatist areas and throughout Georgia. Interdisciplinary approaches are further discussed in Annex D, Coordination for Local Impact.

Third, for the even longer timeframe, the Mission is proposing a coordinated, multi-SO program in the Samtskhe-Javakheti region, a particularly undeveloped area believed to be especially at risk of ethnic conflict and a possible attempt at breakaway such as has already occurred in Georgia. Annex C explains in more detail the conflict prevention and integrated area development concepts proposed for Samtskhe-Javakheti.

Finally, the Mission will continue and possibly expand its support for the South Caucasus Regional Water Management Program (RWMP). The Armenia, Georgia, and Azerbaijan Missions jointly support the long-term study of water management and riparian issues for the South Caucasus’ major river systems. An important (not coincidental) collateral effect is the experience and opportunity this activity presents for officials of these three countries to work together on common problems. The biodiversity assessment update (Annex S) identifies numerous Caucasus activities that foster regional exchange and cooperation. These types of substantive contacts form a foundation for regional conflict prevention. USAID’s support for Eurasia Foundation’s South Caucasus Cooperation Program is similarly justified.

The Mission plans to use Mary Anderson’s seminal work on conflict prevention as an analytical framework and action toolkit.⁶ Anderson advocates a series of analytical steps to understand and mitigate conflict situations, the first being that foreign assistance follow

⁶ Do No Harm: How Aid Can Support Peace - or War. Mary B. Anderson. Lynne Rienner Publishers, 1999.

Hippocrates' challenge to the physician to "do no harm," which, in this context, ensures that we do not inadvertently foment conflict or societal tensions by the choice, management, participation in, or beneficiaries of our development programs. Accordingly, USAID/Caucasus-Georgia will identify and isolate the following factors when considering assistance programs under the new strategy:

- Potential conflict triggers and what would cause them to flare;
- Connectors, or "capacities for peace" that would not break down if a conflict occurred;
- Parties that would be conflicted, their points of view, and potential for resolving their differences; and
- Community peace builders (community leaders, CBOs, NGOs), and their activities on which USAID programs can build.

Explicit Mission attention to conflict prevention methodologies will have positive effects throughout our portfolio. An important new operational tool, the Mission's cross-disciplinary Local Impact Coordination Team, discussed more thoroughly in Annex D, will ensure that conflict mitigation is a central concern of program designs. Focusing on field-level programs operating in a common geopolitical sphere, such as a provincial city or *rayons*, the Coordination Team will help SO Teams marshal consistent mitigation strategies at the community level. Purposely conceived and coordinated, the Mission's array of SO programs is well poised to alleviate the economic, political, and social precursors to ethnic and other communal tensions.

Resources Required: No additional funds need to be programmed to conduct the special conflict mitigation training of SO Teams/partners. However, as noted in Annex C, the following additional resources for the Samtskhe-Javakheti program have been estimated and included in Part IV (Resource Requirements). This activity will command most of the funding requested to address the Cross-Cutting Issue of conflict prevention.

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Provision also is made for continuation of the successor South Caucasus Regional Water Management Program (RWMP) that will bring together the three riparian states: Georgia, Azerbaijan and Armenia. Inter-state river basin disagreements often lead to conflict between the states, and given the separatist issues already plaguing all three states, these additional conflicts can exacerbate this situation. USAID interventions in this Country Strategy seek to continue the dialogue between the three countries that has already contributed to confidence building measures under the current strategy. Resources requested for this activity are the estimated shares of USAID/Caucasus-Georgia. USAID/Caucasus-Azerbaijan and USAID/Armenia have expressed their interest in contributing to and continuing this activity. Note: USAID/Caucasus-Georgia has been managing this regional activity in the current strategy. This activity will receive the balance of the funding needed to address the Cross-Cutting Issue of conflict prevention.

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b. Youth

Problem: Fifteen percent of Georgia's citizens, approximately 750,000 out of an estimated total population of 4.3 million, were born after Georgia became independent in 1991. Georgian youth are a *tabula rasa* on which values, attitudes, prejudices, mindsets, and, most importantly, behaviors are yet to be written and are "editable" in positive ways. The major problems faced by Georgian youth and documented in various studies are: poverty and food insecurity; high unemployment and migration in search of jobs; limited access to health care services; risky life-styles (drugs and alcohol); limited participation in social and political life; a sense of alienation and disregard for societal leaders (values); and lack of exposure throughout their school careers to participatory civic education and programs. These problems are further detailed in Annex H, Youth as a Future Resource.

Children and youth⁷ in Georgia often are found in threatening circumstances linked to the economic/employment status of their families and households. According to the most recent UNDP Human Development Report for Georgia,⁸ 42 percent of couples with children live at or below the poverty line. Even more strikingly, fully 59 percent of household with children headed by single mothers fall below the poverty line in Georgia and more than 25 percent of Georgian citizens are eating less than the minimum caloric requirement. It appears that this problem is more acute in urban areas. A recent USAID-financed household survey⁹ found that urban households are more subject to food insecurity than rural households on a "Food Security Vulnerability Scale." (Rural households fall lower on the "Health Vulnerability Scale" than urban households, conversely, which is its own area of concern.) The USAID-financed survey referenced above also found that 70 percent of Georgian households consider themselves "food insecure." This statistic tracks fairly closely with World Bank projections that 63 percent of Georgian households face the prospect of poverty in the next five years. In short, the harsh financial straits of many Georgian households are particularly stressful for rearing children and youth when food security itself is in doubt.

In urban areas, only 42 percent of the working age population is employed. Two-fifths of these job seekers are under 35.¹⁰ Only 30 percent of 15-24 year old females and 43 percent of 15-24 year old males in urban areas are finding employment. The high rates of educational attainment among Georgian youth therefore quickly dissipate as skills atrophy through disuse. In fact, better educational status correlates with higher unemployment.¹¹ There is less unemployment in rural areas for youth, but job opportunities often are menial. Many, if not most, young adults continue to live with parents, creating family pressures. In major part due to poor employment prospects for many and the difficulty (or under-the-table expense) of accessing opportunities for higher education, Georgian youth often try to emigrate. It is estimated that as many as 800,000 of the older generation of the nineties and other Georgian workers left for job opportunities abroad since independence. This escape valve can only serve to dampen the enthusiasm and commitment of Georgian youth to remain in country and militate for change.

⁷ In USAID's working definition, "youth" includes persons up to the age 25.

⁸ UNDP Human Development Report for Georgia, 2001-02.

⁹ Mult-Sectoral Survey of Households Throughout Georgia. Save the Children. November, 2002.

¹⁰ A Profile of the Labour Market in Georgia. UNDP/IL, 2002.

¹¹ Ibid.

Georgia's youth are increasingly involved in high-risk health and lifestyle behaviors. Road traffic deaths are the greatest single cause of deaths for young people aged 15-25. Eighty percent of Georgian adolescents consume alcohol with some frequency.¹² Emulating Western youth culture, experimentation with drugs is common. Almost 46 percent of young people have experimented with drugs; 30 percent of boys age 10-14 and 62 percent of young males aged 15-19 smoke. HIV/AIDS is an unexploded bomb, with an estimated 2,000 HIV positives,¹³ of which 25 percent are within the 15-25 year age group. High levels of ignorance of safe sex practices adds to the danger, with a UNICEF-supported survey revealing that 43 percent of teenagers have no information on sexually-transmitted infections. Sadly, the difficult economic situation has increased prostitution rates three-fold in Georgia, with as many as one-half being child or adolescent prostitutes. While the GoG is attempting to address all these issues, powerful moneyed interests (such as the cigarette smugglers, traffickers in drugs and persons) will continue to frustrate these laudable public goals.

Between three percent and five percent of youths are actively engaged in politics. Most young people aged 18-25 have no interest in the subject, which echoes western European and U.S. trends. Somewhat surprisingly, alienation from the political process is particularly virulent outside Tbilisi; students in the capital tend to be more apathetic. But even the small politically active minority (more females than males) is primarily "go-fers" for the political parties, and have little or no influence on their platforms or policies. Youth groups outside of politics are few, especially in the regions beyond Tbilisi.

A precise fix on Georgian youths' values and attitudes is more difficult to obtain, as no opinion research specific to youth appears to have been conducted.¹⁴ Informed observers, however, do offer insights. Youth appear to feel a sense of alienation, and have little regard for so-called societal leaders such as politicians. Conversely, young people have favorable views of the West.

Approximately 700,000 Georgian youth are enrolled in grades 1 through 11.¹⁵ Pre-school enrollment (all family-financed) dropped precipitously from 45 percent in 1992 to 20 percent in 1997, most likely due to the economic crisis in many families.¹⁶ Gender access apparently is not an issue. At 2.7 percent and dropping, illiteracy *per se* in Georgia is not an issue. But the overall quality of education is indeed at risk, with under-equipped schools, antiquated curriculum, and ill-paid and ill-trained teachers. On a World Bank index of "real public resources for education", the 1990 reference index of 100 had fallen to 7.7 by 1997;¹⁷ this age group is now in secondary school, at the tertiary level, or will be new entrants in the workforce. The medium term impact on the preparedness of Georgian youth to assume roles as participants in the country's economy and as citizens is obvious. Please consult Annex I, Primary and Secondary Education in Georgia, for a glimpse into the national education crisis.

Strategy: USAID will incorporate activities in all the SOs that will directly benefit youth and will enable them to play an effective role in development. A small number of activities focusing on youth conflict areas also are addressed in the current strategy.

¹² National Tobacco Control Center survey (undated).

¹³ WHO statistics.

¹⁴ USAID/Caucasus plans to undertake a Youth Opinion Survey.

¹⁵ World Bank Education System Strengthening Project Appraisal Document. 2001.

¹⁶ Ibid.

¹⁷ Ibid.

SO 1.31 (Economic Growth) recognizes the latent entrepreneurial talent of young people. The Junior Achievement program will work at the secondary level to instill basic entrepreneurial skills and practical micro-enterprise experience, hopefully whetting the appetite of the young school-leavers for a business career or even business school education at the university level. In addition to teaching simple accountancy, inventory control, marketing, and the rudiments of defining a “business plan”, Junior Achievement more subtly teaches youth concepts of ethical behavior in business dealings and the importance of integrity and responsiveness in non-family, non-clan personal relationships.

SO 1.51 (Sustainable Energy) will make special efforts to mobilize young people, to make them aware of energy production and conservation issues, and to influence attitudes of their parents in targeted communities located inside selected “distribution service areas” (DSAs).

SO 2.31 (Democracy and Governance) and its partners have placed special emphasis on helping Georgian youth understand the basic principles of a “culture of lawfulness” – a new mindset that embraces citizens’ responsibility for accountability and transparency in political and social relationships. Political party development now emphasizes organizing youth wings and a general spirit of youth activism in setting and promoting the issues agendas relevant and appealing to them. Additional initiatives on “civic education” of youth are planned under this SO.

SO 3.4 (Health and Social Development) deals with youth indirectly through its community mobilization program (roughly 50 percent of which is for school construction and rehabilitation) and youth-centered social programs in conflict regions of Georgia, and by overall improvement in their health status. An important segment of our efforts to stimulate public stewardship of communities’ problems will be aimed at the involvement and participation of youth. The scale of community projects (such as school and drinking water system rehabilitation, sports/cultural clubs, small bridge and culvert repair) is well suited to an active youth role, even in the lead role. The SO’s work in health system management and financing at the local level -- an expanded initiative of this Country Strategy -- promises to provide a sustainable foundation for continued improvement in children and youth health beyond the immunization and communicable disease advances of the past decade. HIV/AIDS and STIs, and especially its youth dynamics, continue to receive special programmatic attention in SO 3.4.

USAID will be conducting a Special Initiative in Anti-Trafficking in Persons, which, *inter alia*, will aim at international child and adolescent prostitution rings operating in Georgia.

Broad investments in education by USAID might seem an appropriate youth-directed strategy over the term of the Country Strategy. However, the Primary and Secondary Education in Georgia Sector Assessment (Annex I) documents a major, long-term project funded by the World Bank to entirely revise the curriculum and attendant administrative policies. The magnitude of this effort and USAID’s late arrival in the education sector would argue that “entry points are limited.” Still, the Mission believes that strengthening civic education curricula is within our manageable interest. A Mission initiative in civic education will directly support the broad objectives of SOs 2.31 and 3.4. USAID already has made a modest but significant start with an array of civic education programs. IFES, IRI, ABA, and World Learning all have activities to expose students and young people to

modern civic values. Each of the four “core” SOs will reinforce ongoing civic education activities with new and expanded programs.

Resources Required:

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This youth program focused on civic education may ultimately be managed together with the “youth and democracy” programs anticipated under SO 2.31.

2. Special Initiatives (SIs)

A brief overview of the three SIs is presented below. A detailed description of each SI is presented in Part III, SO 4.1.

a. Elections Assistance SI 4.1.1.

The 2003 Parliamentary elections, and 2005 Presidential elections, hold real promise for Georgia to sustain its nascent democracy. These elections will play a pivotal role either in fulfilling that promise, or they may wind up relegating Georgia to the “failed state” category.

Democratic reform measures and processes have thus far established only a tenuous hold in Georgia. Peaceful, free and fair Parliamentary elections represent a critical first step toward the post-Shevardnadze era. The party or coalition that controls Parliament will dictate the legislative agenda.

In a recent poll conducted throughout the country, fewer than ten percent of respondents voiced faith in either the executive or legislative branches of government. Many youth, Georgia’s future, refuse even to vote, citing stolen votes and politicians who fail to fulfill their promises.

USAID elections assistance is seen as a critical component of our near-term conflict prevention strategy. Conducted without regard to fairness and acceptable electoral norms, the Parliamentary and Presidential elections could simply feed societal tensions and lead to political instability and even adversely affect national security. Great care will be taken to ensure that, above all, we “do no harm.” Recognizing the critical nature of these elections, the U.S. Embassy has declared them its highest priority for USG assistance to Georgia.

In addition to USAID’s programmatic efforts, such measures as high-level political delegations pressuring the GoG for reforms also are needed. Expected results under this SI are presented under SO 4.1.

b. Anti-Trafficking in Persons SI 4.1.2.

This Special Initiative’s goal is to prevent the recruitment of persons living in Georgia from being trafficked for foreign exploitation. Since independence, Georgia has lost over 20 percent of its population who voluntarily left in the wake of deteriorating employment opportunities at home, and desiring to improve their economic situation. While most of

this movement abroad has been perfectly legitimate, some reportedly has resulted in a fraudulent abuse of human rights and values. Traffickers inside and outside Georgia have taken advantage of this situation. Shockingly, no criminal charges have been brought against the alleged perpetrators of these heinous acts, because trafficking *per se* was not a crime in Georgia until the summer of 2003.

No reliable data exist in Georgia to accurately define the scope or severity of the problem. Most anecdotal information indicates that the problem has not yet reached the proportions found in countries such as Ukraine and Russia, where thousands of women are trafficked each year. However, these same sources claim that the problem is growing in Georgia.

The USG has developed a three-pronged approach to the problem of trafficking in persons: **preventing** the problem through improving economic opportunities and warning potential victims of the risks at hand; **protecting** victims through crisis centers, shelters, and other medical and psychological measures; and **prosecuting** traffickers. USAID/Caucasus-Georgia's anti-TIP Special Initiative will focus on the first approach: preventing victims from being trafficked.

The program will begin with a carefully crafted research component, followed by an inventory of all anti-trafficking activities operating in Georgia. Following the initial research and inventory, activities (*e.g.*, public awareness, vocational education and training for victims and vulnerable persons, and policy interventions) can be designed to effectively address the problem in a targeted and meaningful way. Many of these activities can be integrated into existing programs with little or no additional cost.

USAID seeks the following results under this SI: increased national awareness of the problem, legislative and policy interventions, vocational training for victims and potential victims, and gainful employment opportunities through micro-finance programs.

c. Anti-Corruption SI 4.1.3.

Corruption is an endemic “way of doing business” in Georgia. Corruption permeates all levels of government and affects all segments of society. Corruption in Georgia is built on a clan-based system of survival that was refined over the last several centuries. It evolved and became more sophisticated under the Soviet regime. It continues to flourish today.

In 2002, Transparency International's Corruption Perception Index ranked Georgia 85th of 102 countries. Georgia scored 2.4 out of 10, where 10 equates to “highly clean”, and 0 is “highly corrupt”. A 1998 survey of public perception of dishonesty conduct by USAID and the World Bank found that public suspicions of corruption were widespread. The high visibility of corruption in daily life, the lack of criminal convictions despite many allegations of corruption, and the ostentatious shows of wealth among political and business leaders have bred distrust among the public.

Rationale for Treating Corruption as a Special Initiative: The economic costs of corruption for the Georgian society are high. Corruption compounded by low tax collection has adversely affected the GoG's ability to provide essential social services, invest in infrastructure, and pay a living wage to public sector employees. A recent study funded by USAID estimated that in the petroleum sector alone GoG is losing as much as \$220 million annually due to corruption and large-scale smuggling of petroleum products.

Similarly, revenue losses due to smuggling and tax evasion on imported consumer goods are estimated to be in the range of \$120-150 million annually. Left unchecked, corruption in Georgia has the potential to hamper U.S. interests in promoting regional stability, the rule of law, and the integration of Georgia into the larger international community and global marketplace. The goal of sustainable development is not likely obtainable, if the present scale of Georgia's corruption remains unaddressed. Other U.S. interests such as reduction in terrorism and interdiction of the flow of illicit drugs will be unserved, if the criminality bred of corruption is not thwarted.

Most of the programmatic impetus and operational activity in USAID's anti-corruption agenda will be within the Mission's four "core" Strategic Objectives, since this is where the bulk of our resources and our attention reside. Each SO has been carefully reviewed to ensure that anti-corruption objectives are well integrated into the results frameworks.

For results expected under this SI see SO 4.1. The reader is invited to review Annex K, Europe & Eurasia Bureau's Anti-Corruption Methodology (TAAPE) for more insights.

3. Linkages to Agency Policy/Programs

a. Millennium Challenge Account

In FY 2004, a restricted group of 74 countries that are eligible for concessional IDA lending from the World Bank with a per capita GDP of less than \$1,435 (2001) will be eligible to compete for Millennium Challenge Account (MCA) funds. In FY 2005, all countries with a per capita GDP of \$1,435 or less will be eligible. Finally, in FY 2006 all countries with a per capita income of \$ 2,975 or less will be eligible. Georgia falls within the per capita GDP criterion in all three years.

In order to qualify for MCA assistance, countries must (a) be in the top half of all potentially eligible countries according to the "control of corruption" rating from the governance research indicators, and (b) must be in the top half of all potentially eligible countries on at least half of the performance criteria under each of the three dimensions of performance. It is to be noted that MCA legislation is under discussion between the Congress and the Administration, and important details about how MCA allocation rules will work and MCA funded programs will be implemented are still to be finalized. Questions relating to the USAID programs in the MCA countries (funding levels and relationships) also need to be resolved.

From an earlier data set, Georgia would have qualified for MCA funds in its first year of operation. However, as more countries were added to the list of potential recipients, Georgia no longer qualified. According to MCA eligibility, countries are rated according to 16 performance criteria covering three dimensions of performance: "governing justly" (six criteria), "investing in people" (four criteria), and "promoting economic freedom" (six criteria). These criteria are presented in greater detail in Annex R.

According to preliminary rankings, Georgia has met:

- 2 out of 6 criteria under "governing justly"
- 2 out of 4 criteria under "investing in people"
- 3 out of 6 criteria under the "promoting economic freedom"

The criteria still not met by Georgia are:

- civil liberties, political rights, rule of law, and corruption under “governing justly”
- primary education spending and expenditure on health under “investing in people”
- country credit rating, trade policy, and regulatory quality under “promoting economic freedom”

In the second year of the MCA (FY 2005), Georgia would qualify only if the median score counts (ratings) on public primary education spending and public expenditure on health are high enough to pass the hurdle. Present GoG budget trends suggest that this is unlikely.

The new USAID strategy will assist Georgia in meeting the MCA eligibility criteria. However, the currently deficient social sector spending criteria are largely beyond the manageable interest of the USAID program. In the health sector, USAID will help to moderate the lack of adequate public financing by exploring viable financing models that pilot community-based schemes, pre-payment options, and similar approaches in lieu of sole reliance on a national Georgia health plan. In education, our very limited programs, primarily in civic education, will have little or no influence on GoG budgetary allocations directly.

The current programs in the energy sector and private sector development that continue into the new strategy will assist the GoG to develop and implement free trade policies and to promote a market-friendly regulatory environment. In the current strategy (1999-2003), USAID assisted GoG in establishing the Georgia National Energy Regulatory Commission (GNERC) and assisted the National Bank of Georgia (NBG) in implementing several reforms relating to banking supervision and inspection regimes. To the extent feasible, USAID’s Performance Monitoring Plan (PMP) will develop supplemental indicators and measures expressly chosen to parallel the 16 performance criteria underlying the three dimensions of MCA performance criteria. It also may be possible to reconsider Operational Year Budget (OYB) allocations among the SOs depending on the allocation of MCA funds and MCA objectives in Georgia. USAID will examine the coordination needs between MCA and USAID-funded activities as MCA moves into high gear and its implementation modalities are finalized.

b. Global Development Alliance

USAID/Caucasus-Georgia has analyzed the potential for developing public/private partnerships in Georgia under the Global Development Alliance (GDA). As discussed elsewhere in the Country Strategy, Georgia now presents a difficult environment for foreign direct investment and other forms of private sector involvement, both external and internal. The Mission calculates, however, that relatively narrow niches for public/private partnership will exist, and we are poised to exploit them whenever possible to advance our strategic objectives.

The biggest single private investment¹⁸ now underway in Georgia is the Baku-Tbilisi-Ceyhan (BTC) oil pipeline. BP (the former British Petroleum-Amoco) leads the international consortium that has commissioned a Caspian Development Panel to advise on strategies and methodologies for high-impact, people-level development investment along the pipeline route, similar to the socially-, economically-, and environmentally-responsible projects inaugurated along West African pipeline rights-of-way in the last few

¹⁸ \$ 2.9 billion over the entire three-country pipeline route.

years. This Panel is in addition to the more modest Community Investment Program (CIP) for the pipeline communities to which BP already is committed. The Panel is exploring with USAID how to crystallize an enhanced multi-donor¹⁹ partnership with the GoG and the pipeline route communities. The Mission's decision to develop a conflict prevention program in the Samtskhe-Javakheti region of southern Georgia, perhaps also including Azeri communities in the southwest, overlays well BP's geographic area of emphasis. If BP were to bring such development resources to the table, these would easily meet the GDA's matching criteria. A likely timeframe for the Panel's recommendations to BP for the Georgia program would be late calendar year 2003.

Other public/private partnership potential exists elsewhere in the USAID/Caucasus-Georgia program. The Support Added Value Enterprises (SAVE) activity in SO 1.31 (economic growth), discussed below, is designed to attract private sector co-investment in agribusiness marketing, equipment leasing, and production system services. The Microfinance activity in the same SO will develop credit programs with the private sector Georgian banking community. ABA/CEELI remains active in rule of law programs in our democracy and governance SO 2.31. Winrock is a partner with USAID under the Georgia Energy Security Initiative to develop energy solutions for rural communities. The Mission's Georgia Community Mobilization Initiative (GCMi) is helping rural communities implement local infrastructure improvements chosen by them; a Rural Works activity under consideration might take this a step further through creation of road user associations. And the SO 2.31 team has conceptualized an activity for the new strategy period, which would create municipal/private sector partnerships to tackle obstacles to SME growth and development at the local level.

USAID, the World Bank, the Ministry of Finance, and the Georgia Social Investment Fund (GSIF) have entered into an arrangement whereby USAID GCMi resources will be used to lay the ground work for subsequent leveraged investments in local infrastructure. This initiative is discussed below in the SO 3.4 narrative, section J.

c. Values

Georgia's elite historically has identified itself with Western cultural values despite their accommodation to centuries of tyrannical regimes imposed by neighbors. While espousing European ideologies, Georgia remains today a volatile mix of ethnic-clan allegiance, an undying belief in welfare entitlements, and nascent democratic institutions. In response, the Country Strategy's sub-goal rightly aims to "foster new values and attitudes that encourage citizens of Georgia to be responsible and accountable for the direction of their country."

In the Georgia of today, Western ideals of fair business competition, democratic governance, free speech, and individual dignity contrast sharply with the reality of organized crime, autocratic officials, muffled dissent, and failure to protect human rights. Few Georgians have been exposed to how public institutions and a free electorate are expected to interact in terms of accountability and responsibility in contrast to older democracies where such behaviors are taught throughout primary and secondary school curricula. Constituents and officials alike will need to learn that effective governance is a two-way street with responsibilities and accountability shouldered by both parties. It is hoped that these democratic norms can be nurtured in a peaceful, pluralistic manner while

¹⁹ Including UNDP, and the World Bank's Georgia Social Investment Fund.

safeguarding the rich cultural diversity of Georgian society. The Country Strategy addresses this gap by proposing programs to promote the understanding and practice of democratic procedures and heritage among youthful citizens.

The need for civic values training is recognized in the design of all four of the Mission's core SOs. For example, open business **competition** championed by SO 1.31 must confront smugglers, rent-seeking inspectors, and an un-level playing field. These behaviors discourage domestic and foreign investments. **Trust** in government institutions, as best seen in the country's energy crisis handled by SO 1.51, must deal with state-sponsored embezzlement, consumers who feel entitled to free electricity, and Parliamentarians who interfere in the affairs of independent regulatory bodies. The corruption of governmental processes erodes legitimacy of authority and jeopardizes the future operation of the energy sector. **Disclosure** and free and open debate supported by SO 2.31 must defend freedom of speech, laws on the media, and fair elections. Without the value of tolerance the "tyranny of the majority" will oppress minorities and allow irrational passions to hold sway. The **right of assembly** seen in SO 3.4's programs of civic mobilization must deal with an inexperienced citizenry, empty municipal coffers, and appointed national advisors who ride roughshod over the decisions of elected town officials. Community-based organizations are transforming the old Soviet attitude that communities must passively wait for top-down central government decisions. The grass-roots approach embraced by this Country Strategy will apply the basic values that Georgians have long espoused but have rarely practiced.

Additional thoughts on the inculcation of values are found in Annex J, Values Analysis.

d. Graduation

USAID program "graduation" is difficult to foresee at the present time. Rather than a fixed timetable, we believe that readiness for graduation must be measured by whether or not Georgia's transition has achieved a self-generating momentum, independent of stimulus from the donor community. At the national governmental level, the GoG has been thoroughly exposed to international "best practices" in macroeconomic management, finance, and democratic processes. Readiness for graduation at the national level, therefore, is already guided by the informed choices that political leaders are fully capable of making. Yet, readiness at the "local" institutional level is more problematic, mostly because sufficient capacity is still lacking.

Minimum conditions or pre-requisites for genuine graduation are captured below for each of the four "core" SOs:

- SO 1.31 (economic growth): Basic financial infrastructure for a market economy is in place, with a sustainable banking system gaining public confidence and credit available throughout Georgia. Higher-value agricultural exports are increasing exponentially in at least two industry "clusters" to neighboring countries through WTO frameworks and EU agreements.
- SO 1.51 (sustainable energy): Electricity supply reaches 100 percent of forecasted demand plus a reserve margin including interconnects with regional countries. Energy generated or produced²⁰ is transparently accounted for, billed for, and

²⁰ Natural gas and electricity.

collected, with corrupt diversions and major customer non-payments under control. Social, financial, and environmental concerns regarding energy operations/investments are addressed by reliably independent regulatory agencies.

- SO 2.31 (democracy and governance): At least 70 percent of the population is engaged with responsive local governments that listen to citizens and other stakeholders and provide the services and policies they demand, in particular through a professional and transparent budget and revenue expenditure process. Citizens are able to organize themselves and advocate effectively for their needs.
- SO 3.4 (health and social development): The economy is able to generate sufficient revenues to cover critical social needs. The health system has transparent costs; flexible risk-pooling financial arrangements are in place for private citizen contribution, and the GoG finances a “basic benefits package” for vulnerable populations.

USAID’s global experience and the Mission’s experience to date in Georgia suggest that graduation from U.S. bilateral development assistance is not reasonably attainable for ten years after Parliamentary and Presidential elections. At the earliest, the presence of a transparent and accountable government is not expected until 2015. The objective measures for graduation status would be attainment of the goal and sub-goal indicators at performance levels equivalent to those of the Central European and Baltic States at the time of their accession to the European Union (EU).

PART III: PROPOSED COUNTRY STRATEGY

Strategic Objective 1.31 Accelerated Development and Growth of Private Enterprise to Create Jobs

A. Statement of Strategic Objective

Strategic Objective (SO) 1.31, Accelerated Development and Growth of Private Enterprises to Create Jobs, builds on the current SO 1.3 (Strengthening Private Sector Growth and Development) and seeks to consolidate the gains accomplished to date. USAID programs under this SO stimulate further strengthening and development of the overall private sector in Georgia, while emphasizing export-oriented agribusiness development and micro-finance programs as driving forces for employment generation. USAID analyses indicate that there are several aspects of private sector development where progress is still needed to achieve this Strategic Objective. These aspects constitute three Intermediate Results (IRs): 1) Improved Policy and Operating Environment; 2) Increased Access to Financial Services; and 3) Increased Market-Driven Production and Sales.

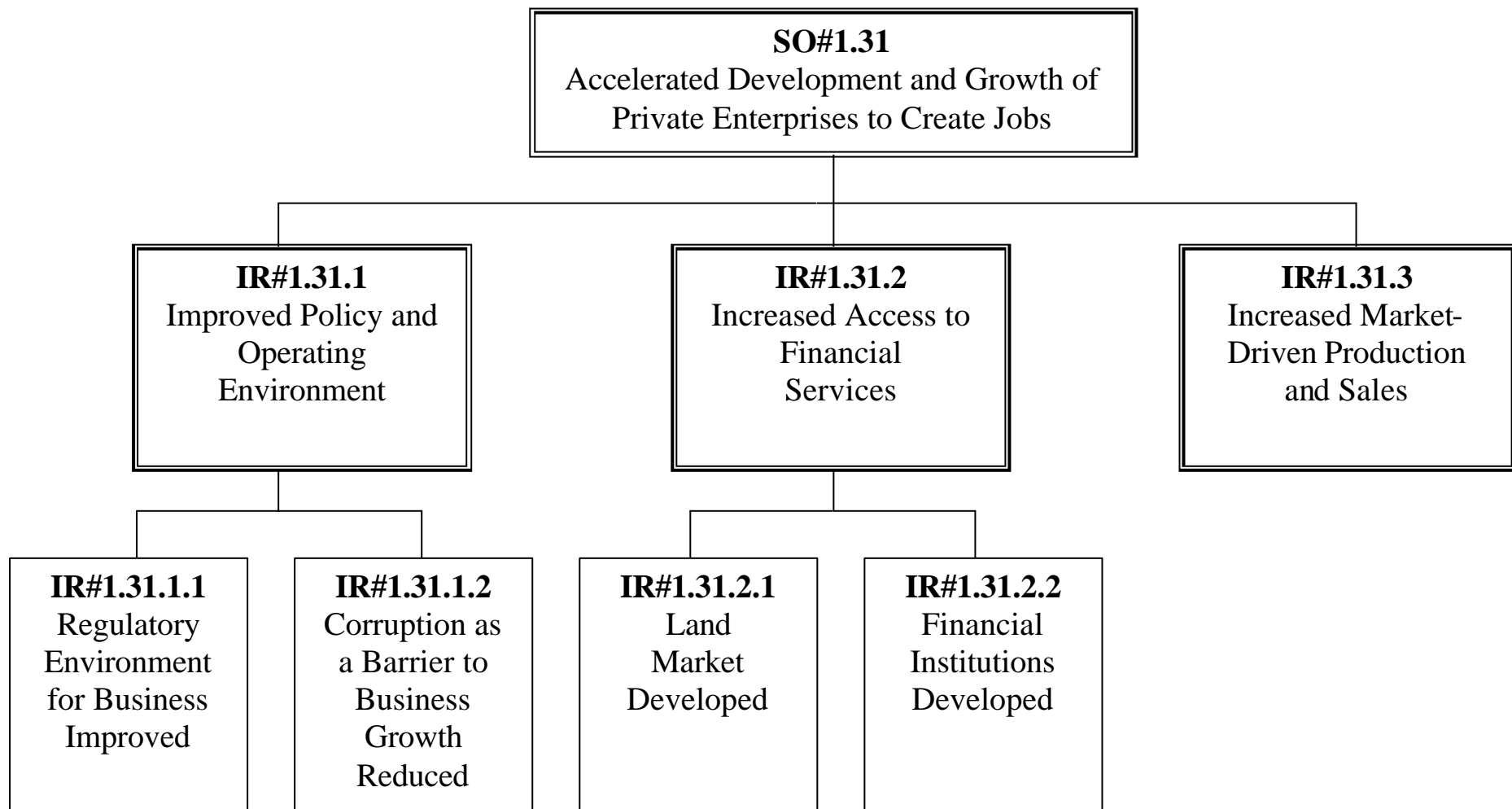
B. Problem Analysis

Georgia's economy has gradually collapsed since independence. By 2000 its real GDP had fallen to 29 percent of 1990 levels, the worst decline in the former USSR. Two-thirds of Georgia's population lives in poverty. Unemployment runs at 30 percent. Per capita GDP is approximately \$700 per annum. The Georgian economy is concentrated in a few sectors and is in need of diversification. About 75 percent of GDP growth is concentrated in communications, financial services, and transportation, whose share of total employment is less than five percent. Georgia's largest exports are in air transport, scrap metal, gold, and wine. Imports are concentrated in oil, medicines, and gas.

Georgia is primarily an agriculture-based economy. Agriculture contributes about 19 percent of GDP. Fifty percent of employment is concentrated in this sector. The agricultural sector has been neglected and its potential to contribute to increased exports, employment, rural incomes, and poverty reduction has not been addressed in any significant manner. Large state-run, agro-processing enterprises inherited from the former Soviet Union are now defunct. Due to lack of agribusiness and marketing skills among the Georgian entrepreneurs, exports have suffered severely and Georgia has lost its traditional markets. There is a critical need to recapture the lost markets for agricultural exports. The overwhelming majority of enterprises in Georgia are micro-enterprises, mostly in the informal economy, that depend on micro-finance. Credit for SMEs is scarce, with very high-interest costs and collateral requirements. There is a large, unmet demand for micro and SME credit. Foreign direct investment, very limited as it is, has been concentrated in the energy sector, wine, and telecommunications and has been dismally low at about \$120 million in recent years.

Although the private sector generates more than 60 percent of all economic activity in Georgia (jobs, income, trade and exports, services, tax revenues), it has been facing major constraints: pervasive corruption, state subsidies to yet-to-be privatized industries, lack of transparency in government dealings, weak system of contract enforcement, an unsatisfactory judicial system, onerous business licensing procedures, harassment by

USAID/CAUCASUS-GEORGIA SO 1.31 RESULTS FRAMEWORK



regulators, and absence of property registries. The Tax Code favors a few private interests. These obstacles discourage private sector development and investment -- both domestic and foreign. Regrettably, however, corruption and lack of real reform have slowed the process of private sector development and discouraged investment.

Programs started in FY 2003 seek to ameliorate several problems noted above. USAID's broad, multi-year economic growth program that began in June 2003 includes demand-driven policy and regulatory reforms in banking and fiscal policy administration; further consolidation of banking sector reforms; land reforms; and building private sector capacity for policy advocacy. In supporting policy reform, USAID seeks to create a predictable and transparent environment for trade and commerce, including a fair and efficient system of tax collection and application of laws and regulations. Two follow-on programs to improve agribusiness competitiveness and access to credit also will begin in FY 2003. The first one (SAVE – II) will support increased market-oriented production by removing constraints to the development of value-added market-targeted products especially in the agricultural sector. The second will expand access to credit; will further strengthen the capacity and outreach of the financial sector, including micro-finance institutions; and will promote the use of land as collateral for credit.

C. Development Hypothesis and Rationale

The SO is built on four underlying hypotheses:

- The only way to create sustainable jobs and reduce poverty is to promote economic growth through private sector development;
- Demand-driven policy reforms pursued in partnership with the private sector will be more successful in driving sustainable changes in the policy and business operating environment in Georgia than isolated technical assistance provided directly to State institutions
- Improving financial infrastructure (including micro-finance institutions) will help mobilize capital, increase access to credit and financial services, and spread the benefits of growth to a broader range of the vulnerable population; and
- Production and sales can be stimulated by removing constraints that prevent enterprises from focusing on products and services demanded by markets. The demand-driven approach to production and marketing is particularly important in countries with a Soviet legacy.

D. Critical Assumptions

Four critical assumptions are posited for SO 1.31:

1. There will be no external shocks so great as to destabilize the civilian government;
2. The internal separatist movements will not worsen during the strategy plan period;
3. The GoG will not reverse constructive policies already in place; and
4. The GoG will respond favorably to pressure from civil society including the private sector.

E. Progress to Date (1999-2003)

Since 1996 USAID supported reforms in the following areas: tax and fiscal policy, accounting, land privatization, capital markets, and business development. However,

implementation of reforms has been uneven and in some cases has been slower than expected.

Despite concerns regarding the health of the banking sector as a whole, USAID's bank supervision activity helped the National Bank of Georgia (NBG) take critical steps to improve Georgia's financial sector. These included: mandatory use of International Standards by commercial banks, increased capital requirements, laws on Asset Classification, Conflict of Interest, and Internal Audit and the development of electronic, inter-bank payments system to provide real-time settlements between the NBG and commercial banks. As a result, confidence in the banking sector has increased, and real value of deposits, while still low, has doubled in the past two years. With assistance from USAID, over 530 Georgian enterprises adopted International Financial Reporting Standards.

USAID provided technical assistance to the Tax Department to fairly and efficiently enforce tax laws, increase government revenues, improve transparency, ensure taxpayer compliance, and develop a tax system more conducive to private sector growth. Computerization assistance will allow the Georgian Treasury (Tax Department) to consolidate 12,000 accounts into one; implement a complementary audit selection model; and requires that all tax payments go through the commercial banks. The reorganization of the Tax Department along functional lines has been completed. Tax inspectorates in regions and at the headquarters have been computerized and linked through a communications network.

The land privatization program supported by USAID has been a major success. By June 2003 the program will have completed surveys, registration, and titling of more than 2.4 million parcels of agricultural land, which constitutes about 25 percent of all farming areas. This enables the smallholders, generally impoverished rural households, to use the land as collateral for credit, and represents the beginning of a functioning land market. Secondary transactions in the land market are doubling annually.

Three USAID micro-finance program implementing partners (Constanta, FINCA, and ACIDI/VOCA) have established models of successful lending by providing a range of innovative loan products to micro, small, and medium-sized businesses, maintaining an average national repayment rate of nearly 98 percent. These institutions are making steady progress toward operational and financial sustainability. Of more than 25,000 active borrowers, 75 percent are women. Assuming a ratio of 1.5 jobs per loan, this accounts for the creation/maintenance of over 37,000 jobs, mostly among vulnerable populations.

With assistance from USAID, Georgia gained membership in the World Trade Organization in 1999 and completed the restructuring of the Ministry of Agriculture, which will help Georgia to meet EU and WTO export standards. The Support Added Value Enterprises (SAVE) project was launched in 2002 to assist Georgian agribusinesses to develop and export value-added agricultural products. The first phase of this project had focused on identifying constraints to the development of agribusiness, preparing market analyses to identify opportunities for agricultural exports and import substitution, and testing interventions for removing processing and export constraints. Phase II of the project focuses on processing and marketing, and began in FY 2003.

F. Program Approach

1. Expected Results and Illustrative Activities

- 60% increase in registered private enterprises from 2004 to 2008; and
- 80% increase in jobs created by USAID's SO 1.31 assistance activities.

Three IRs will accomplish SO 1.31:

IR 1.31.1: Improved Policy and Business Operating Environment. Priorities for a national business agenda are expected to begin emerging from private sector partners. Technical assistance will ramp up to support priority needs identified by the private sector related to policy, financial infrastructure, and competitiveness. The Georgia Enterprise Growth Initiative (GEGI) will be USAID's principal resource for addressing these priority needs. Two sub-IRs (IR1.31.1.1 and 1.31.1.2) will accomplish this IR.

IR 1.31.1.1: Regulatory Environment for Business Improved. The regulatory environment will be improved through the following illustrative activities.

Illustrative Activities:

- Continue support for promotion and fair application of the tax code;
- Assist courts of arbitration to increase use of alternative dispute resolution;
- Assist Georgia to prevent adulteration and trademark violation of selected products;
- Assist Georgia in replacing mandatory standards with voluntary standards;
- Assist Georgian entities to conform to selected priority WTO standards and protocols;
- Assist the Ministry of Finance in tax and customs policy and administration;
- Develop simple, centralized systems to establish businesses and conduct inspections; and
- Assist in addressing commercial law and policy reform.

Other regulatory issues will be addressed as they emerge on a demand-driven basis during the course of program implementation.

IR 1.31.1.2: Corruption as a Barrier to Business Growth Reduced. Anti-corruption activities are integrated throughout the SO 1.3 program. The primary approach is to utilize business associations and public-private partnerships to ensure that State policies and practices provide a level playing field for business and eliminate the burdensome extra-legal payments endemic in Georgia today. The private sector will be strengthened to serve as an independent monitor of public sector activities, as a watchdog of corrupt practices, and as forceful advocates for a crack-down on corruption. The SO strategy will seek to reduce corruption through five possible activities.

Illustrative Activities:

- Developing public-private partnerships to eliminate corruption (*e.g.*, effort to combat smuggling of oil products);
- Reducing corruption in the banking sector through rigorous banking supervision;
- Reducing fraud through establishment of a company registry, collateral registry, and credit information bureau;
- Publicizing land registration requirements and set up transparent procedures; and

- Streamline agricultural product inspection regimes to reduce bribe-taking opportunities.

IR 1.31.2: Increased Access to Financial Services. Over the strategy period, the Mission will support increased access to financial services by focusing on land markets, micro-finance and rural credit, and other types of financial infrastructure. This IR will be accomplished by two sub-IRs (IR1.31.2.1 and IR1.31.2.2).

IR 1.31.2.1: Land Market Developed Following the successful completion of the titling and registration of 2.4 million small land plots, the USAID land reform program is currently negotiating with the GoG to privatize larger State-owned plots, which make up about a third of all arable land in the country.

Illustrative Activities:

- Legislation for privatization of State-owned agricultural land is to be presented to the Parliament soon; and
- Assuming this legislative project goes forward in the near term (and if not, further legislative advocacy will continue until it is achieved), USAID will continue to support the initial implementation and set-up of standards for titling and registration of these economically viable plots.

IR 1.31.2.2: Financial Institutions Developed

Illustrative Activities:

- The banking infrastructure program started under the current Country Strategy will continue through May 2004, ensuring that the National Bank of Georgia (NBG) is capable of sustaining the implementation of improved bank supervision systems.
- The Georgia Microfinance Stabilization and Enhancement activity will provide technical assistance and grant funding in support of micro and small enterprise finance in both urban and rural markets to ensure the long-term sustainability of the institutions, including the ability to attract additional donor funds.
- Going forward, the Georgia Enterprise Growth Initiative (GEGI) will address key financial infrastructure issues such as an integrated company registry, collateral registry, credit information bureau, and other initiatives supported by the private sector.

IR 1.31.3: Increased Market-Driven Production and Sales. The Support Added Value Enterprises (SAVE) project will enable the production, processing and export sale of selected Georgian agricultural products through the identification and mitigation of critical constraints. Having completed initial research, the implementation phase of the activity starting in FY 2003 will support five key activities.

Illustrative Activities:

- Creation of an import/export trade brokerage service;
- Establishment of a leasing company;
- Construction of a pilot processing facility for selected products; and
- Support for agricultural services.

- GEGI includes a competitiveness component that will support selected pilot non-agriculture cluster development efforts over the strategy period.

2. Performance Indicators

At the SO level overall progress in achieving the results of SO 1.31 will be measured by two indicators:

- a) Increase in number of private enterprises (registered). While official statistics are neither comprehensive nor reliable, they at least show the trend and indirectly provide evidence for the creation of new jobs; and
- b) Number of jobs created attributable to SO 1.31 activities. This indicator will use activity-level information supplied by SAVE and the cluster component of GEGI. A standard index will be applied for jobs created by MFI loans (1.5 jobs per borrower). This indicator will be disaggregated by gender, location (Tbilisi/regions), and age (25 and under/over 25).

At the IR level the following results are expected:

- a) Improved Policy and Business Operating Environment (IR1.31.1): will be measured by Country Credit Rating (“International Investor” Magazine);
- b) Regulatory Environment for Business Improved (Sub-IR 1.31.1.2): will be measured by two indicators: i) Regulatory Index (World Bank); and ii) Days to Start a Business (World Bank);
- c) Corruption as a Barrier to Business Growth Reduced (Sub-IR 1.31.1.2): i) A composite index of corruption developed in GEGI ii); and Revenues generated by the oil revenue enhancement effort;
- d) Increased Access to Financial Services – Real value of loans by commercial banks and USAID-assisted NBFIs;
- e) Land Market Developed (Sub-IR 1.31.2.1): i) Number of loans outstanding using land as collateral, disaggregated by gender; and ii) Number of land parcels sold (registered transactions) disaggregated by location (Tbilisi/regions);
- f) Financial Institutions Developed (Sub-IR 1.31.2.2): i) Real value of deposits (including current accounts, time deposits of enterprises, household, and other demand deposits); ii) Weighted average of financial and operational sustainability of targeted non-banking financial institutions (NBFIs); and iii) Number of active borrowers in USAID-assisted organizations, disaggregated by gender, location (Tbilisi/regions), and age (25 and under/over 25); and
- g) The best available information to track the progress in IR 1.31.3, Increased Market-Driven Production and Sales, will be Export Sales Volume (excluding scrap metal), (approximating the country’s competitiveness and inflow of hard currency).

G. Linkages to Other SOs, Cross-Cutting Issues, and Special Initiatives

SO 1.31 will work with SOs 1.51, 2.31 and 3.4 to promote and establish public-private partnerships in the energy sector and community-based business development activities. Energy sector stakeholders (SO 1.31) will also be actively engaged in demand-driven policy reform and preparation of the National Business Agenda under the GEGI project. Similarly, in implementing activities focusing on youth and dealing with anti-corruption efforts, SO 1.31 will coordinate and leverage activities, information and resources with all other SOs.

H. Resources Required and End Date

The following annual resources are requested to accomplish the results under SO 1.31:

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SO 1.31 is anticipated to continue in its current form until September, 2013. Further support may be necessary in a new form.

I. Sustainability

Sustainability is built into every aspect of the SO 1.31 strategy. On the policy side, the shift to working with private sector associations and groups to support reform is a more sustainable alternative to government-to-government assistance, which too often has ended with collapsed initiatives when donor funds dried up. The private sector will be a constant force supporting a stable policy and operating environment. Nevertheless, building sustainability into associations and policy advocacy activities is a long-term undertaking.

Efforts in banking supervision have been aimed at increasing the sustainability of the banking sector, and while further consolidation is required, the sector is on track toward that end. Likewise, USAID-supported micro-finance institutions already are operationally sustainable, but additional work over the strategy period is required to improve their institutional stability. While USAID may contribute start-up costs for needed financial infrastructure, all such efforts will be designed to be ultimately self-sustaining.

Production and sales-enhancing efforts in agriculture and other sectors are being designed with sustainability in view. For this reason, they are market-driven and targeted at removing constraints, rather than starting with production and offering subsidies. USAID endeavors to create conditions in which Georgian entrepreneurs can sell products to real markets, ensuring that increased private sector activity, will continue after assistance ends.

J. Other Donor Programs and Impact on SO Results

The World Bank, EBRD, European Union and KfW (Germany) support SME development with technical assistance, grants, and loans. USAID coordinates closely with the KfW and GTZ on land privatization and land market development activities. While the World Bank and IMF are expected to continue to support fiscal reform, and the U.S. Treasury will continue assistance to the Tax Department, USAID assistance will be considered where there are opportunities with government entities that are ready and willing to reform. USDA and the World Bank plan to provide complementary support to USAID's agribusiness competitiveness activities. The EU, IMF, EBRD and IFC assist the commercial banking sector with technical assistance and loan capital for on-lending, efforts that complement USAID's programs in the financial sector.

K. Activities Not Supported

In the proposed strategy USAID will provide limited direct assistance to the GoG. In the past, technical assistance has been less effective due to lack of commitment by GoG

counterpart institutions. A second shift is away from support for equity markets. Despite substantial USAID support in the past, equity markets in Georgia remain illiquid, with a low level of trade in stocks and bonds, and with little prospect for growth in the foreseeable future.

Strategic Objective 1.51 A Foundation for a Sustainable Energy System

A. Statement of Strategic Objective

Strategic Objective (SO) 1.51, A Foundation For a Sustainable Energy System, builds on SO 1.51 (A More Economically Efficient and Environmentally Sustainable Energy Sector) in the current strategy and seeks to consolidate several gains accomplished to date. USAID programs under this SO seek further strengthening and development of private-sector-led energy production, supply and distribution systems, while supporting the GoG in the development and implementation of market-friendly energy sector policies and regulatory frameworks. USAID analyses indicate that there are many aspects of energy sector development where progress still is needed to achieve this SO. Three Intermediate Results (IRs) are necessary to accomplish the SO: 1) improved financial and commercial performance of energy sector entities; 2) a more diversified, renewable and cost effective energy supply; and 3) increased environmentally-sustainable energy efficiency.

B. Problem Analysis

Despite a sound regulatory framework, knowledgeable middle management, and major donor support, Georgia's energy sector has become increasingly dysfunctional due to systemic corruption, physical asset deterioration, inconsistent enforcement of regulations, and consumer distrust. Energy sector reforms in Georgia have not attracted hoped-for private investment nor increased service reliability. Attempts to attract private investment to all levels of the sector have been largely unsuccessful due to investor awareness of infrastructure degradation and gross mismanagement of the sector.

An overwhelming problem of the Georgian energy sector is failure to collect a substantial portion of energy charges from consumers. Collection rates remain low, especially from state-owned enterprises (SOEs). Abusive political influence, lack of law enforcement, and conflicting government policies combine to ensure that procedures and rules put in place to disconnect non-payers are rarely applied to individuals and corporations with political clout. Theft, misappropriation of collections, primitive billing regimes, corruption and public attitudes are major problems affecting collections. Currently 78 percent of the funds needed to cover electricity costs are "lost". Some 35 percent disappears due to theft (of power and collected revenues) and vandalized meters, 30 percent to arrearages and un-collectibles (*e.g.*, separatist Abkhazia and S. Ossetia), and 13 percent is not recovered due to offsets and non-transparent barter agreements. This leaves only 22 percent of expected revenues to run the entire national electricity grid. Due to allegations of embezzlement, few of the actual collections ever return to the generating entities or to the GoG's transmission and dispatch company (GSE) for urgent maintenance and repairs, resulting in frequent breakdowns, further deterioration in installed capacity, and mounting unpaid salaries. The attitude of "entitlement" of the institutional consumers -- especially government ministries and state enterprises -- and the public at large has been another major problem. Georgian energy consumers display a lack of personal accountability to pay for energy consumed, at the same time as disowning any sense of responsibility for the financial situation of the energy sector as a whole.

Over the course of the current Country Strategy, USAID became acutely aware of the problems with collections by the distribution companies and the lack of hardware, software, and management systems to address these problems. Pilot work on metering, billing and collections highlighted a willingness of consumers to pay bills for reliable power in some areas. There was also resistance to pay in areas where power was available around the clock. Thanks to the “unbundling” of the sector into separate generation, transmission and distribution companies, it was found that the distribution companies were not making payments to the generation companies. For example, the United Distribution Company (UDC), created through the consolidation of 65 smaller companies, paid virtually none of the \$1.5+ million it collected in January 2003 for the purchase of bulk electricity. Not surprisingly, electricity shortages remain a continuing problem every winter due to infrastructure deterioration, as well as a lack of cash to purchase electricity and gas from neighboring states to meet peak seasonal demands.

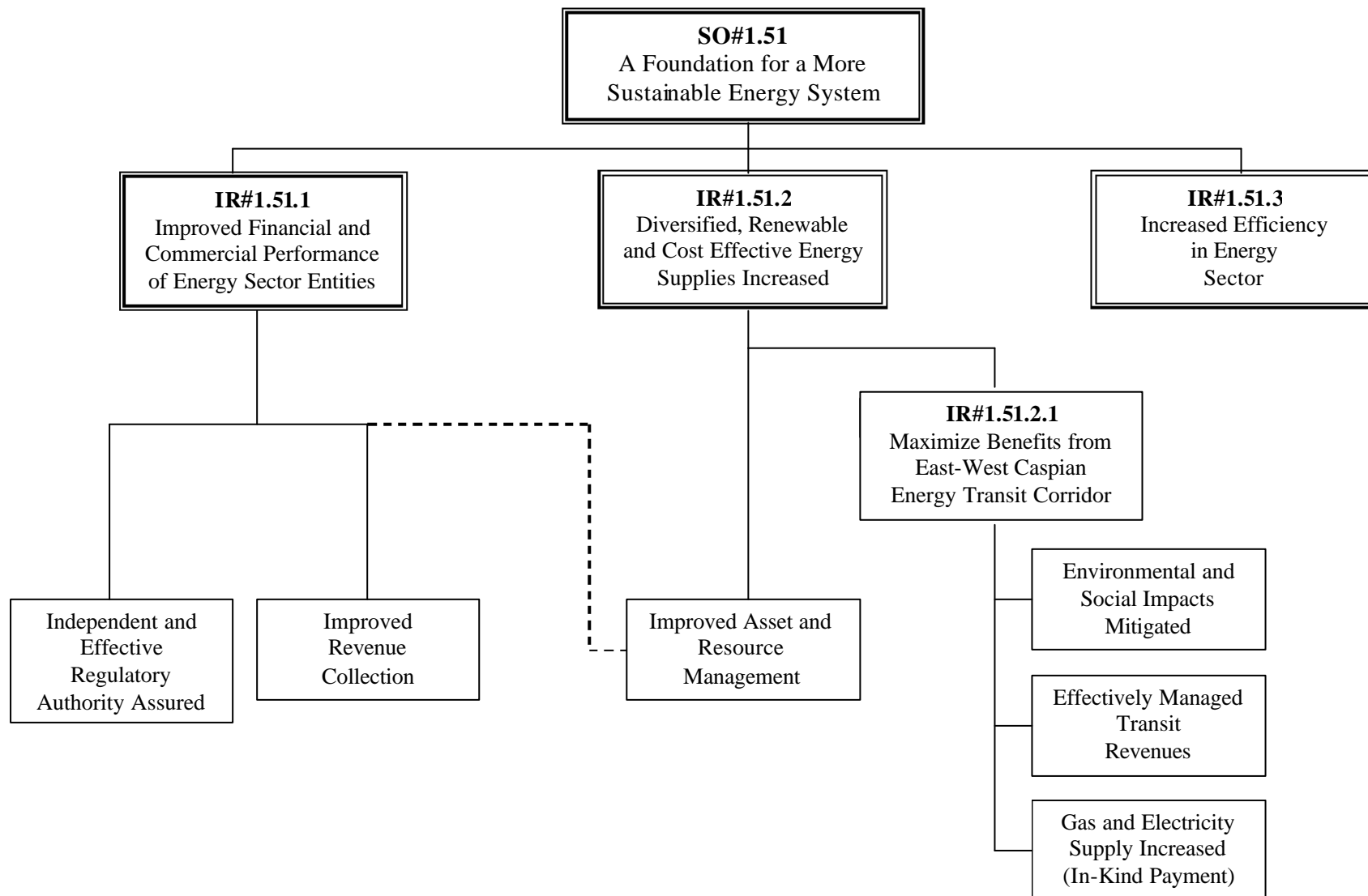
The solution to these problems must come from consumers themselves. Enforcement, prosecution, and midnight patrols of meter police alone will not prevent theft. Consumers have to be persuaded to prevent theft, increase payments, and accommodate fair and transparent tariffs in exchange for institutional accountability, depoliticized rate-setting, investor confidence, and reliability of supply.

Due to continual infrastructure degradation and the lack of short-term liquidity to purchase power from outside of Georgia, peak winter demand for electricity regularly outstrips supply. Rural areas suffer the most. Some areas outside the capital have no power for weeks or even months. Outages are due partially to a technical absence of power and partially to administrative disconnections for non-payment. The problem limited to winter months now threatens to become a “24/7/365” phenomenon. A 1998 energy investment plan identified rehabilitation of the existing hydropower resources as the lowest cost investment to increase Georgia’s installed electrical capacity. While other donors are financing investment in the largest hydropower plant (Enguri) and transmission infrastructure, USAID will focus on physical restoration of smaller and medium-sized hydros and assist underserved communities to meet their energy needs through the development of alternate energy sources.

Power outages and shortages are endemic, especially during winter months when it is critically needed. Alarmed by the poor electricity supply and space heating shortages during the winter of 2000-01, the GoG convened an Energy Working Group (EWG) to address the persistent difficulties. By June 2001 the EWG had developed a comprehensive power sector rehabilitation strategy and shared it throughout the GoG. In early 2002 the Ministry of Fuel and Energy drafted its own “Georgian Energy Security” document. A key objective shared by both plans is to deliver uninterrupted electricity supply to all paying customers by late 2005.

During 2001-03 the GoG demonstrated little enthusiasm to implement reform, as typified through interference and lack of respect for the independence of the regulatory bodies charged with implementing the legislative reform in place. Success throughout the energy sector is predicated on these institutions functioning well. However, institutional support to these key regulatory organizations will continue whenever conditions permit. This will depend on clear evidence of commitment of GoG leadership in all branches (executive, legislative, and judicial) to a financially-sustainable power sector.

USAID/CAUCASUS-GEORGIA SO 1.51 RESULTS FRAMEWORK



In spite of the serious problems facing the energy sector, the Mission is cautiously optimistic that key improvements in the sector will be forthcoming in 2003-04. The IMF has conditioned its first loan tranche on acceptable management contracts for electricity transmission/dispatch and the wholesale power clearinghouse. As these are performance-based contracts, continued improvement in electricity supply and application of market-based rules remains an achievable goal over the next five years, provided there is less negative government intervention and the GoG commits itself to meaningful sector reform. USAID project disbursements also are linked to IMF conditions. Future USAID technical assistance will promote commercialization of gas and electricity distribution companies through (1) improved management, (2) increased operational efficiency and reliability, (3) improved retail collections, and (4) reliable payments to producers (through GWEM) and the dispatcher (GSE).

C. Development Hypothesis and Rationale

For the long-term health and sustainability of the energy sector, supply and demand for power must be brought into better balance, and the reliability of power better assured. Responsible consumer behavior cannot emerge until the consuming households and SOE managers see the impact of a financially viable and reliable power system at the personal and corporate level. This realization requires a two-pronged strategy: revitalizing viable power entities at the consumer level, and ensuring at least a minimum level of effectiveness of national/regional regulatory, financial and infrastructural entities. We expect that conditionality, coordinated among the donors, will eventually leverage the necessary implementation of institutional reforms designed and promoted by USAID. In the interim, it is essential that we have demonstrable successes “on the ground” of a) reliable, viable power delivery to meet consumers essential requirements, and b) communal stewardship through public awareness and participation related to payment for that reliable power.

D. Critical Assumptions

1. Political and economic stability maintained/improved. Energy has become a contentious political issue as Georgia approaches the fall 2003 Parliamentary elections. It is assumed that the political environment will not be so volatile that we would be unable to address needed reforms, such as paying a fair share for reliable power.
2. Government acknowledges and works to correct financial insolvency. Virtually all major entities in the sector have negative cash flows, have irresolvable debt burdens, or are otherwise technically bankrupt. GoG actions need to reflect a clear commitment to address the mounting indebtedness, the erosion of asset value, and the negative impact of VAT.
3. Reform-minded leadership emerges. New legislative and executive leadership at the national level will emerge to implement reforms and sustain those already implemented.
4. Abusive governmental interference reduced. All levels of the GoG have been known to direct that electrical services not be disconnected for certain politically important customers (*e.g.*, Georgia Railways), thereby providing free power in return for political favors. The electorate must hold such officials to account.

5. Public participation replaces public apathy. Consumers are willing and able to become active partners in rebuilding a sustainable energy sector at the local, regional and national level.
6. Donors remain committed. It is critical that donors maintain a strong, unified commitment to sectoral reform, and that they enforce conditionality while dealing with the GoG.
7. Pipelines built on time. To maximize the economic benefits of the trans-Caucasus oil and gas pipelines, it is critical that they be built on schedule.
8. USAID resource levels sustained. SO 1.51 achievement depends on requested levels of funding being available over the five-year Country Strategy.

E. Progress to Date (1999-2003)

USAID assistance helped to significantly restructure Georgia's energy sector. Key legal, policy, and institutional reforms were enacted. A foundation was laid for reorientation of the Georgian energy entity from state ownership to a privately-owned, well-managed sector. A critical part of the sector was privatized. The power sector was unbundled. The independent oil and gas oversight agency and the electricity and gas regulator promulgated regulations necessary for private investment opportunities. Management contracts designed to instill transparent commercial practices in generation and transmission were initiated with critical input from USAID. The GoG retains ownership of 2,500 MW of hydropower resources of which less than half -- 1,100 MW -- are technically operable. Several successful demonstration projects for management reforms, collections improvements, and energy efficiency were completed. Regrettably, however, the GoG has seemingly abdicated its responsibility to implement its own regulations despite considerable outside pressure and numerous reports from domestic watchdog organizations.

To ensure that the most vulnerable Georgians did not bear the brunt of a still-incomplete and imperfect privatization process, USAID first financed the Georgia Winter Heating Assistance Program (GWHAP) in 1998-89. Begun as a humanitarian project for IDPs "temporarily" housed in hotels and public buildings, GWHAP now subsidizes the winter heating bills for low-income households. GWHAP has been extended every year since its inception. Through a series of offsets, credits to the beneficiaries' accounts results in cash available to the electricity sector of Georgia.

As privatization and full-pricing take hold, many residential electricity consumers accustomed to "free" or subsidized electricity service are shifting to the cheapest fuel source available -- firewood -- with alarming environmental damage.

Transition to the new SO 1.51: Under the current Country Strategy, SO 1.51 focused on the privatization of energy sector entities. Recognizing that sectoral reform has stalled, USAID identified major payment bottlenecks and breakdowns tied to problems with regional governance. Also, inefficiencies in SOEs have become more evident, and assets have dwindled due to alleged embezzlement by a chain of takers from local electricity distribution companies down to the individual bill collectors at the household/enterprise level. In response, the balance of resources and even the geographic emphasis of the new SO will shift to community-based, decentralized efforts to re-engineer the technical, managerial, financial and social dynamics of the energy sector. The new SO aims to improve the efficiency, accountability and transparency of distribution, and, where applicable, to place the production and transmission entities on a commercial footing in preparation for eventual privatization, while developing consumers' active support for

and responsibility in achieving these reforms. “Commercialization” implies running operations at lowest long-term costs, covering accrued debt, and investing in the sector for sustainability and reliability of supply. Parallel to its commercialization efforts, USAID will continue its support to the nascent national regulatory organizations charged with ensuring the independence and regulatory oversight of the sector and ensure that they are able to respond to consumers’ legitimate concerns and needs.

F. Program Approach

1. Expected Results and Illustrative Activities

- Electricity and as sector revenues approach parity with sector costs; and
- Gap between electricity demand and electricity supplied narrows sufficiently to ensure basic power reliability.

Both SO-level accomplishments will require surveys to establish baseline and to track progress.

Three IRs will accomplish SO 1.51:

IR 1.51.1: Improved financial and commercial performance of energy sector entities.

Improved financial and commercial performance of energy sector over time will regain the confidence of energy sector investors.

Illustrative Activities:

- Upgrading metering, distribution, billing and collection systems plus advisory services to electricity and gas distribution systems;
- Increased public awareness of energy issues;
- Public energized to insist on financial accountability and an end to corrupt practices at all power system and governmental levels;
- Capacity-building of the regulatory institutions; and
- Evaluation of the GWHAP project and its transformation into a sustainable social safety net.

IR 1.51.2: Diversified, Renewable and Cost-Effective Energy Supplies Increased.

Illustrative Activities:

- Emergency repairs to avoid further technical collapse;
- Training and other assistance to generation and distribution companies to improve asset and resource management;
- Technical assistance to increase investments made in renewable energy at the community level; and
- Advisory services to identify and recommend steps to establish credit facilities to finance community investments.

Sub-IR 1.51.2.1: Maximize Benefits from East-West Caspian energy transit corridor

Timely completion of the energy corridor will help ensure new gas supplies that render regional monopolies less effective. To protect this new supply, communities need to have a stake and derive economic benefits.

Illustrative Activities:

- With USAID technical advice and assistance, pipeline builder (British Petroleum) funds Community Investment Programs for infrastructure repair, sustainable income generation, water supply, and environmentally sustainable energy sources;
- USAID-funded Georgia Community Mobilization Initiative provides complementary investments at the community level, and
- USAID technical assistance to GoG in establishing an Oil Revenue Fund (ORF).

IR 1.51.3: Increased Efficiency in the Energy Sector

Households, enterprises, and communities shift from inefficient energy sources and technologies to more efficient ones. As revenue collections are enforced, it is crucial that customers have the information and funds available to invest in more efficient technologies or to switch to other, more cost-effective and environmentally-sound sources of energy.

Illustrative Activities:

- Fuel substitution projects at the community level to include environmental programs that reduce use of firewood and increase the use of efficient wood-burning stoves; and
- Credit programs to underwrite investments in energy efficiency and renewable energy sources at the household, enterprise and community level.

2. Performance Indicators

Two indicators will measure success at the SO level: 1) electricity and gas sector revenues approach parity with sector costs (an indication of operational sustainability); and 2) the gap between electricity demanded and electricity supplied narrows sufficiently to ensure basic power reliability. It is to be noted that in the wake of many years of energy sector disruption, that it is difficult to ascertain what constitutes market-clearing demand. Non-payments, vandalized meters, and technical shortages combine to make it a challenge to estimate true demand. Currently estimates are the total electricity supply is 60 percent of demand. Similar levels are not known for gas supply.

IR 1.51.1: Improved financial and commercial performance of energy sector entities.

Indicators: 1) Gap reduced between kWh billed to end-use customers and kWh received from the wholesale sources; and 2) Gap reduced between kWh billed and kWh collected for gas and electricity delivery (an additional measure of commercialization of distribution companies).

IR 1.51.2: Diversified, Renewable and Cost-Effective Energy Supplies Increased.

Indicators: 1) Actual operable installed hydro megawatts over total installed megawatts (hydro and non-hydro) (a measure of improvement in locally generated and renewable sources of supply); and 2) average cost of kWh delivered (a measurement of the cost efficiency of aggregate supply).

Sub-IR 1.51.2.1: Maximize Benefits from East-West Caspian energy transit corridor.

Indicators: 1) BP funds CIP along the east-west Caspian Energy transit corridor; 2) community-level infrastructure improved; and 3) GoG establishes the ORF and transfers funds to communities.

IR 1.51.3: Increased Efficiency in the Energy Sector.

Indicators: 1) number of more efficient and cost-effective energy sources installed; 2) consumption patterns (volume and sources of energy) of target groups show conservation; 3) reduced use of wood (in target communities); and 4) increased use of renewable energy. An energy consumption survey may be required.

Areas to monitor for anti-corruption activities follow:

- Establishment of a clear legal framework and autonomous, transparent and accountable regulatory body with sufficient authority;
- Unbundling of the power system into multiple entities – transmission companies and multiple distribution and generation companies with transparent commercial practices;
- Establishment of decentralized electricity market arrangements including competition and direct decentralized payments between distribution and generation companies through credible commercial banks to reduce cash transactions to energy companies;
- Privatization to eliminate the direct access to most of the flow of funds and control by government officials and make it more difficult for political interference in the process;
- Improved management of distribution companies.; and
- Increased public awareness of energy issues.

G. Linkages to Other SOs and Cross-Cutting Issues

SO 1.51 will work with communities to foster local responsibility for their own energy needs through community mobilization, including local councils to initiate community-financed energy projects. These efforts will be coordinated with SO 2.31's civil society and local governance activities. Similarly, community mobilization programs of SO 3.4 will be leveraged to ameliorate community energy constraints. Private sector participation in community-financed energy projects, entrepreneurial training, and demand driven energy policy will be coordinated with SO 1.31. At the national level, the SO 1.51 program directly targets corruption through transparent commercialization and eventual privatization in ways conducive to the national interest. Effective regulatory watchdogs such as GNERC, buttressed by an aroused and articulate citizenry, are central to this strategy.

H. Resources Requested and End Date

USAID is requesting ----- for SO 1.51 over five years:

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The end date for SO 1.51 will be no sooner than September, 2009.

I. Sustainability

Sustainable progress is dependent on the creation of a more secure technical, financial, and regulatory foundation. Six criteria at a minimum are necessary:

1. Societal and environmental concerns regarding energy operations and investments are addressed by appropriate regulatory agencies, in partnership with private companies and public review;
2. Supply equal to 100 percent of forecasted demand plus a reserve margin (15-25 percent for electricity, depending on interconnectivity with other countries' systems);
3. A policy on disconnections and enforcement of said policy;
4. All segments of the system (generation, transmission and distribution) billing and collecting 100 percent of revenues due;
5. Minimum theft and bad debts and prosecution of documented theft; and
6. Electricity and gas rates equal to total revenue requirements (including cost-effective investments to improve efficiency and a small amount for bad debt) plus a margin which balances societal and investors' interests.

J. Other Donor Programs and Impact on SO Results

The success of SO 1.51 is tied directly to World Bank, EBRD and KfW activity in this sector.

- World Bank and KfW are together lending \$39.8 million (78 percent of the project cost) for transmission and dispatch upgrades and the GSE management contract.
- EBRD is granting \$1.2 million (29 percent of the cost) for the GWEM management contract and 60 percent of the cost of the Enguri Hydropower Dam rehabilitation.
- KfW is conditioning a \$34 million loan to rehabilitate the Vartsikhe power dam on the submission of a business plan demonstrating a positive rate of return sufficient to cover all costs through revenue collections. Pending receipt of such a plan the KfW is willing to use \$5 million of the proposed loan for emergency repairs. Likewise, the funds could be used for long-term management contracts conditioned upon more progress in sectoral reforms. KfW also is deliberating with the GoG to finance mini hydro, but it is unclear whether these negotiations will bear fruit. KfW also has expressed interest in partially funding a five-year private UDC management contract that will follow on behind USAID technical assistance to UDC begun in May 2003. No other bilateral donors (grant-making) are involved in the energy sector.
- The management contracts for GSE and GWEM already are in place, so there is no threat of delay. However, their implementation could fail due to weak GoG commitment. If this failure occurs, it will compromise the twin goals of increased collections for the hydro power plants through GWEM and GSE and enforcement of disconnection policies.
- USAID, other bilateral energy donors, and IFIs coordinate their efforts periodically to optimize leverage on the GoG to complete much-needed fundamental reforms in the sector.

K. Activities Not Supported

Major new investments in generating or transmission capacity, including improved interconnects with regional electricity systems, are not perceived to be within USAID's manageable interest or budgetary resources, and in any event may not be timely in the absence of political commitment to a financially viable power system. At the other end of the scale, major investments in alternative energy sources (*e.g.*, biomass, energy efficiency) do not seem to be the solution to the gross energy needs of the Georgian economy unless and until the continued dysfunction and distorted economic signals in the power sector are successfully addressed. USAID will, however, actively explore

alternative energy models, especially in rural, “off-grid” areas presently or potentially less impacted by the unresolved issues in the power sector discussed above. We hypothesize that -- by improving management and infrastructure and by emphasizing the link between paying for and receiving power -- pressure will be brought to bear on the GoG to reduce its political interference and proceed with implementation of the reforms.

Strategic Objective 2.31 More Effective, Responsive and Accountable Local Governance

A. Statement of Strategic Objective

Strategic Objective (SO) 2.31, More Effective, Responsive and Accountable Local Governance, addresses Georgia's democracy and governance reforms, which continue at an uneven pace.

The Georgian Parliament has passed some of the most progressive reform legislation in the former Soviet Union, which has laid the groundwork for meaningful change. The Administrative Code, coupled with its Freedom of Information section, represents some of these advances. Leading citizens are learning to effectively lobby for change. In June, 2002, Georgians democratically elected their mayors in all but two cities in elections that were deemed chaotic but largely free and fair. Local government reform is underway, and political parties are slowly evolving beyond "personality cults" to craft messages that appeal to constituents. This modicum of progress has been hard-won, and gains continue to be threatened.

Plagued by a post-Soviet legacy, elected local officials are subordinate to appointed regional officials and depend on central government transfers, which hamstrings local governments while supporting clientelism and corruption.

Although the judiciary has shown itself independent and has ruled against the government at the national and local levels, the executive dominates the legislative branch, which limits democratic oversight and representation. Loyalties of the legislature are defined by ties binding Parliamentarians to the President and the clientelistic web of political-economic interests that surround him. Many Georgian politicians, including the President, talk volumes about combating corruption, but no one seems capable or willing to attack the problem. This complex web results in stalled reforms and halted progress.

B. Problem Analysis

Georgia's democratic development is stalled at the national level, where corruption, lingering Soviet behaviors and political competition combine to stymie reform efforts. Except for the judiciary, which has proven itself to be reform-oriented from the top down, opportunities for reform are more easily found at the local than the national level. The current development challenge in Georgia lies in identifying key opportunities with the judiciary and with local institutions and enabling them to take root. Georgia will flourish only when citizens insist that the government adequately respond to their demands for justice.

In 2004-2008, USAID will maintain its focus on local governance, but with an emphasis on a comprehensive community stakeholder/local government engagement, anti-corruption, and youth and democracy. By design, democracy interventions will be conceived as one single programmatic effort with four related elements, all focused to achieve the same purpose. These four elements include local government reform, increased citizen participation, independent media, and rule of law. All four elements work together to achieve improved local governance in communities.

Two of these components form the central theme of SO 2.31: reforming local government and increasing citizen participation. These components are two sides of a supply-and-demand “coin”: citizens demand meaningful change to improve their lives, and local government responds. Both elements require significant interventions to achieve targets. Citizens must learn to organize themselves, to advocate for their interests, and to lobby government for their needs. Youth, Georgia’s future, must play an increasingly vibrant role in this process. Political parties need to represent constituents. At the same time, locally elected officials must learn to respond to citizens, efficiently deliver key services, and rebuild communities.

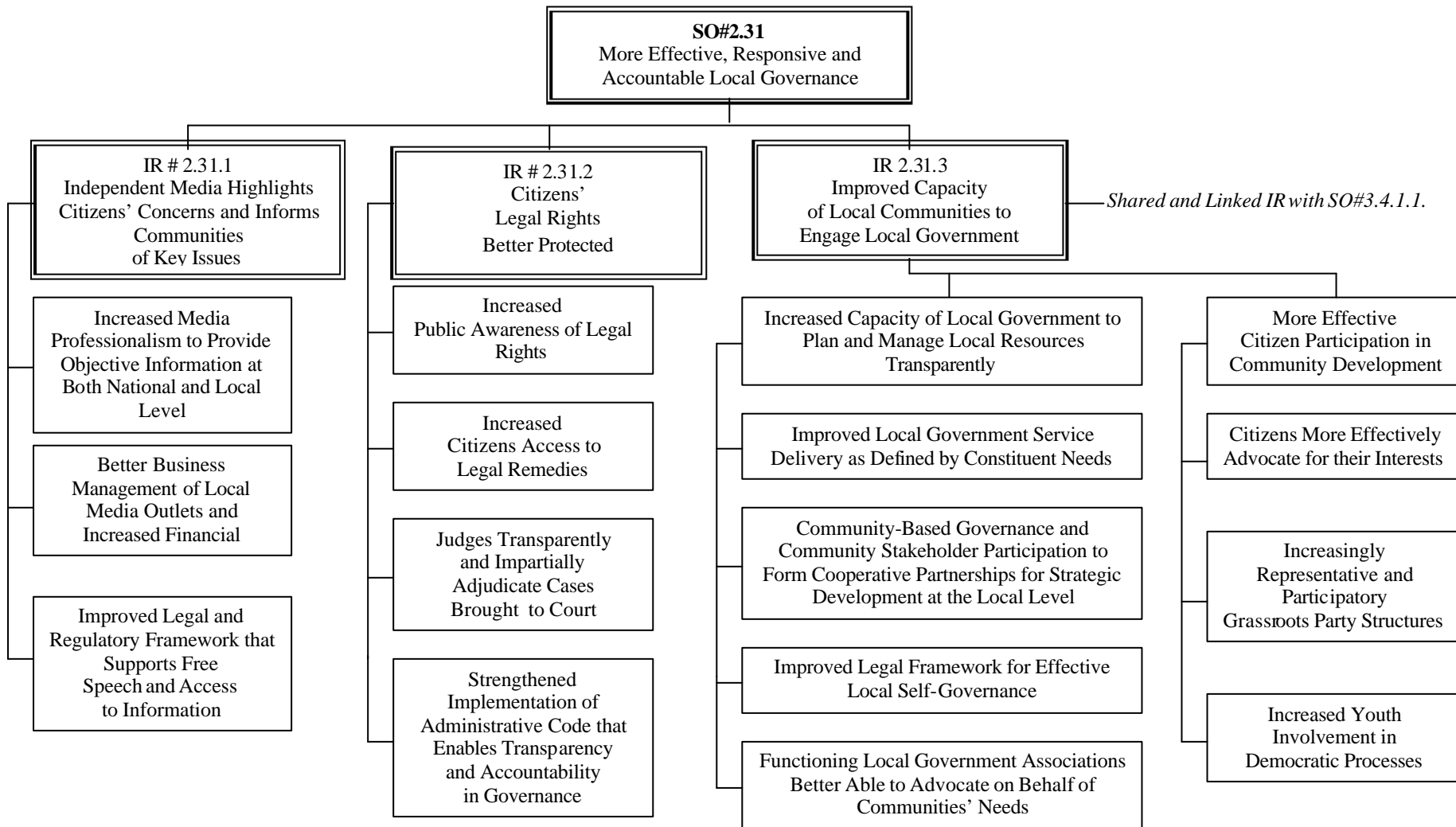
The USAID-assisted legal services program will be refocused on preventing encroachment by the State on democratic freedoms. Similarly, we will strengthen implementation of the Administrative Code to emphasize those provisions that check the arbitrary exercise of power by executive branch personnel at both the national and local levels and to hold government more accountable. Administrative Code reform now needs to focus on those elements that have a positive, near-term, and visible impact on citizens’ redress.

Until recently, citizens' contact with the administration of justice generally had been frustrating and sometimes frightening. The vast bulk of the population still thinks of the legal system, including the courts, as a method for the government to control and punish rather than as a protector of citizens against government abuse. However, with successful reforms in the judiciary, the courts have begun ruling in favor of citizens against the government. Citizens who have actually used the courts report a greatly enhanced perception of the courts and of private lawyers. USAID plans to continue providing assistance to the judiciary, to help it further develop as an institution. Such assistance will include a phase-in of case management, which will help the judiciary function more efficiently and also make judicial processing more transparent and less subject to petty corruption in scheduling. Because the judiciary must also play a key role in any anticorruption effort, USAID will provide assistance at the national and local levels to help judges better understand patterns and practices that indicate corrupt actions by government bureaucrats. USAID also will provide such material assistance as seems appropriate to enable the courts to cope with their caseloads and information needs.

Independent media comprises another major component of USAID's re-crafted democracy and governance strategy. We have redesigned this program element to focus on citizen-identified concerns and access to information on key issues. In addition, the Mission will continue to assist Georgian media to become more professional, help media outlets to be better managed and foster an improved media legislative and regulatory environment.

Anti-corruption weaves as a Cross-Cutting Issue throughout SO 2.31. Citizens acting individually or through NGOs must hold government officials accountable, using the mass media to publicize problems and successes, and the courts to achieve rights given by Georgian and international law. The judiciary must understand what forms corruption takes and must be willing to support citizens when justice is on their side. Citizens and the mass media, in turn, must keep watch that the courts function transparently and impartially. Informed and demanding citizens, free and competent mass media, and an honest and independent judiciary all must play their proper roles to curtail corruption in Georgia.

USAID/CAUCASUS-GEORGIA SO 2.31 RESULTS FRAMEWORK



C. Development Hypothesis and Rationale

USAID proposes to minimize its democracy and governance reform efforts at the highest levels (Parliamentary, ministerial, and national initiatives) because of a mounting number of discouraging reversals: failure to adopt election roll reforms, Parliamentary reduction in electricity tariffs to garner votes in the upcoming elections, and inadequate efforts to meet IMF performance indicators. This “supply side” approach to reform has experienced serious backsliding over the last two years. Therefore, USAID intends to address similar issues using a “demand side” rationale where better informed, effectively organized constituencies insist on fuller disclosure and responsiveness from their elected representatives. A strategy focused on communities also stands a better chance to discourage corruption: activities are scaled to be more manageable, understood by all parties, and have clear, near-term outcomes benefiting identifiable members of the community.

The rationale underpinning a renewed emphasis on “grassroots” community development is threefold. One, the fewer the layers between voters and their elected leaders, the more responsive officials will be. Two, increased disclosure and scrutiny by peers will reduce the frequency and scale of corrupt behaviors. Three, the more active citizens are at the “grassroots” level, the more likely that they will ultimately participate in higher level regional and national political processes.

Admittedly, SO 2.31 narrows the democracy and governance spectrum. Rather than focusing on national-level institutions *per se*, USAID will build democracies from the ground-up, beginning at the local level, and including youth in these efforts. (One of USAID’s major continuing efforts is to increase youths’ active involvement in issues-based political party development.) Likewise, major legal reforms that do not directly address local issues may well fall outside USAID’s newly defined manageable interest. This integrated strategy will strengthen USAID’s democracy and governance portfolio by incorporating best practices of past endeavors without reaching beyond what can reasonably be achieved in Georgia.

D. Critical Assumptions

1. National-level corruption can be successfully attacked but remains a central problem.
2. Georgian Parliamentarians will continue their squabbles with the executive branch at least through the 2005 Presidential elections, effectively stalemating “supply-side” reforms.
3. Meaningful reforms will be most evidenced at the local level on a case-by-case basis.
4. USAID funding levels will remain constant or decline only modestly.

E. Progress to Date (1999-2003)

Three major new interventions were launched, strengthening the focus on a nascent reform effort. The Local Governance Reform Initiative (LGRI) began in September, 2000, and is now active in five cities. Independent evaluators urged the Mission to expand LGRI to larger urban areas and deepen its focus to include a more comprehensive community-based development model. “Citizens Advocate!” and “Media Innovations” programs were launched in 2002, directly responding to recommendations of the 2001 civil society assessment. “Citizens Advocate!” awards grants to more sophisticated NGO coalitions who lobby the government for meaningful reforms with a strong presence in

regions outside the capital. “Media Innovations” strengthens print and broadcast media outlets outside Tbilisi through technical assistance and grants, while also drafting legislative proposals and lobbying for Parliamentary reforms. Rule of Law (RoL) programs supported implementation of judicial reform and were geared to strengthen Georgia’s legal profession. Also, RoL focused on the implementation of the Administrative Code, with its ground-breaking Freedom of Information section. Public awareness campaigns on legal rights were conducted, and legal service organizations were expanded to seven regions. In the election arena, USAID instigated a major initiative to improve election administration, including piloting Georgia’s first electronic voter registry in three regions.

Transition to the New SO 2.31: USAID’s democracy and governance program will deepen its focus on community-level impact. Three themes resonate in this re-crafted strategy: better coordinated local governance, anti-corruption, and youth. The reasons for this re-emphasis are clear: all assessments and evaluations under the current Country Strategy note that “grassroots” efforts are the most sustainable and often more free from corruption. Interventions at the community level also present the target of greatest opportunity -- and represent the greatest need. Georgia’s youth comprise a critical resource for building a vibrant democracy. USAID’s restructured democracy and governance program will retain its former elements (local government reform, increased citizen participation, independent media, and rule of law) but will concentrate these elements at the local level with a stronger emphasis on anti-corruption and youth. The former SO 2.2 for Legal Systems will be folded into the recrafted SO 2.31. In addition, USAID’s new Country Strategy includes a Special Initiative for elections assistance rather than incorporating this component in SO 2.31.

F. Program Approach

1. Expected Results and Illustrative Activities

- Index of public satisfaction with local governance rises from 50 to 80% in targeted areas;
- Percentage of citizens aware of their legal rights rises;
- Judicial independence and effective case management improve;
- Index of local government transparency and access rises; and
- Advocacy campaigns conducted by community service organizations (CSOs) increase.

The first accomplishment is the prime index that captures the overall rapport between citizen and town officials. Measurements for the secondary accomplishments will be part of PMP development.

Three IRs will accomplish SO 2.31:

IR 2.31.1: Independent Media Highlights Citizens’ Concerns and Informs Communities of Key Issues. Increasing the ability of the independent media in Georgia to effectively highlight citizen concerns and inform communities will be achieved by strengthening their independence and professionalism through several activities.

Illustrative Activities:

- Assist in the improvement of the legal and regulatory framework to support free speech and access to public information;
- Assist in improving the management skills and practices within the media industry to ensure functioning of media outlets as efficient, profit-seeking businesses;
- Improve journalistic skills within the industry to ensure that citizens are provided with objective, balanced and fact-based information; and
- Assist in ensuring that supporting institutions, such as professional and trade associations truly promote the professional interests of independent media.

IR 2.31.2: Citizens' Legal Rights Better Protected Protection of citizens' right remains a fundamental principle for achieving rule of law in Georgia. Various activities are focused on the demand and supply side of citizen's interaction with the state in seeking justice. Several activities aim to achieve the IR.

Illustrative Activities:

- Public awareness campaigns to increase public knowledge of legal rights;
- Strengthening legal profession and support for free legal services to increase citizens' access to legal remedies;
- Strengthening judiciary as an institution, improving case management, judicial training, support for association of Judges of Georgia to achieve better adjudication of cases brought to the court; and
- Support for demand for and supply of information under the provisions of the General Administrative Code to ensure transparency and accountability in the executive branch

IR 2.31.3: Improved Capacity of Local Communities to Engage Local Government. The ability of local citizens to effectively engage and positively influence their elected local governments will be increased through several activities.

Illustrative Activities:

- Providing grants and mentoring from nationally based Georgian NGO's to regional and local NGO's that increases local NGO's advocacy skills based on forming grassroots networks of citizens and community groups;
- Continue to assist local governments and municipalities to adopt formal regulations for open council meetings that included agendas being published in advance as well as time placed on the agenda that allow citizen comments/participation;
- Assist in the formation of community partnerships to ensure that local government decisions reflect citizens' interests and were made in cooperation with all stakeholders in the community (citizens, business, energy, and etc.);
- Assist in formal adoption of local regulations that promote transparency and community access to all decisions, budgets, and ordinances passed by local governments; and
- Number of major political parties with functional offices to sustain community outreach in targeted Districts

2. Performance Indicators

The retailored SO 2.31 has indicators similar to interim indicators approved in 2001, reflecting the fact that the Mission's democracy and governance program is already

focused at the local level to a significant degree. Specific indicators, detailed in the preliminary Performance Monitoring Plan include: an index of public perception of local governance in targeted districts; percentage of citizens aware of their legal rights; judicial independence and effective case management; an index of local government transparency and access; and advocacy campaigns conducted by community service organizations (CSOs).

In 2004, USAID plans to launch two major new democracy and governance programs. First, a new ----- project entitled Constituents Engaged in Local Decision-Making (CELD) will build on the Local Governance Reform Initiative's success to implement a more community-based approach to reinstate basic services in several Georgian cities. Second, a ----- cooperative agreement will combat corruption through a multi-faceted approach based on USAID's current TAAPE methodology. Some of these interventions currently are being tested; the most effective approaches will be included in the new program and will be managed in coordination with the anti-corruption team in the Regional Legal Advisor's office. Work with youth also will continue. A mid-term evaluation of the current school-based civic education program will be conducted with a follow-on program to start in 2005.

Discussion of Anti-Corruption Activities

This SO addresses two sides of community development: the supply side of local governments and the demand side of citizen interests. Anti-corruption efforts integrate into both parts.

Evidence from Georgia's regions demonstrates that the level of corruption is significantly diminished at the local level. Two reasons may account for this finding: (1) smaller stakes in those communities simply have fewer resources to entice major graft; and (2) more accountability, since Georgia's communities are small, with an inter-connected population. People are more aware of corrupt practices in their midst, and perhaps tolerate less. Moreover, local officials were democratically elected and therefore more accountable to their constituents.

Three pillars of assistance comprise the strategic objective: media, legal rights and community development. This last pillar includes both local government interventions and citizen action. Anti-corruption activities are woven into each of these pillars.

Illustrative anti-corruption activities include the following:

- Independent media highlights citizens' concerns and informs communities of key issues. Media offers a powerful tool to highlight community concerns, such as anti-corruption. Interventions will include public service announcements, public information campaigns, and investigative journalism to focus attention on corruption and galvanize demand for it to stop.
- Judges transparently and impartially adjudicate cases brought to court and strengthened implementation of the Administrative Code that enables transparency and accountability in governance. Judges must be free from corrupt practices in order to adjudicate cases impartially. Georgia's Administrative Code with its Freedom of Information section allows citizens access to government budgets and enables them to attend government meetings. Watchdog NGOs can monitor budgets, and citizens can openly interact with government representatives

to lobby for their concerns. These methods comprise powerful anti-corruption tools.

- Community-based economic development process created. This process involves all citizens working together in an open and transparent manner to jointly craft community development plans. Rent-seeking will be exposed and squelched in such a transparent process.
- Improved legal framework for effective local self-governance. One of the most critical legal reforms needed to empower local governments is a law on revenue. Decentralizing Georgia's revenue process, enabling local governments to both collect and retain taxes, will reduce graft in the system. These actions can be complemented by an open and transparent system on the local level of a budget development and adoption process where citizens are invited to participate through open hearings and meetings.
- Citizens more effectively advocate for their interests. Interventions will result in citizens better articulating and lobbying for their interests. Activities could include support for legal clinics to assist victims of corruption. Free legal advice could be given to citizens about their rights related to alleged corruption and excessive bureaucracy including legal expertise on government agency filing procedures necessary to request formal investigation, and the provision of legal support in court to victims of corrupt practice.

G. Linkages to Other SOs and Cross-Cutting Issues

It is recognized that several elements in the SO 2.31 framework closely correspond to sub-IRs within complementary SO 3.4, which also focus on increased capacity to deliver social services identified by communities. This close link is noted in their respective Results Frameworks.

Youth can play a dynamic role in Georgia's democratic process; but before they can help their country move forward, they must have a vision for what their country can become. Building a "Culture of Democracy" forms a critical component of Georgia's long-term development.

H. Resources Requested and End Date

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Programs in democracy and governance will extend to September, 2013. After Presidential elections in 2005, the Mission intends to reassess the development environment to determine whether meaningful results can be achieved at the national level.

I. Sustainability

New institutional relationships must be nurtured to sustain SO 2.31. Four elements are critical to sustainability:

1. Elected municipal officials will be endowed with a measure of independent fiscal authority and responsibilities;
2. Appointed officials from the national levels and seconded to the regions will fill largely advisory and technical roles;
3. The electorate will be accustomed to holding local council officials to account; and
4. Cynicism and apprehension will give way to hope and conviction.

J. Other Donor Programs and Impact on SO Results

USAID funding comprises the lion's share of democracy and governance assistance in Georgia. However, two other significant donor-funded efforts are underway:

- The World Bank Municipal Development Fund (WB MDF) plans to encourage LGRI pilot cities to compete for MDF funding, and will incorporate LGRI-type training into their activities. A delay in WB MDF funding would slow the spread of USAID-conceived community development efforts and diminish hard-won influence over this sector.
- The Council of Europe (COE) is currently working on local government reform legislation as well as municipal association development. Currently the COE and USAID's LGRI project are coordinating recommendations for draft legislation on decentralizing municipal property transfers. The absence of COE efforts would weaken our residual presence in the "supply side" of the democracy and governance sector.

K. Activities Not Supported

USAID will continue supporting reforms in the legal realm. However, rather than have a "stand-alone" SO, the Mission will integrate RoL elements into the rest of the democracy and governance portfolio. The RoL program will continue to focus on protecting citizens' legal rights and judicial effectiveness and transparency, but with an increased emphasis on local-level implementation.

Strategic Objective 3.4 Catalyze Improvement of Social and Health Services in Targeted Areas

A. Statement of Strategic Objective

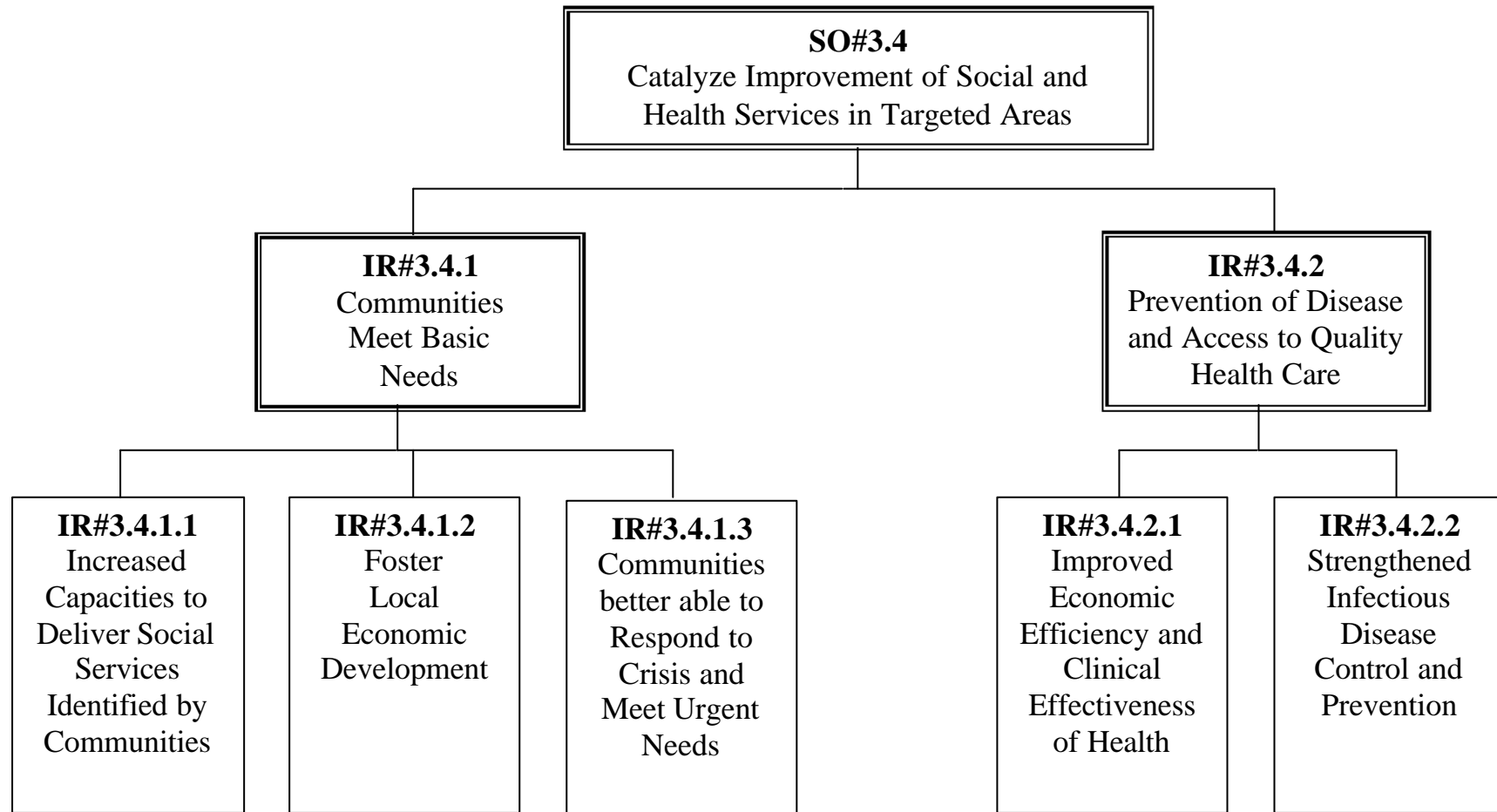
Strategic Objective (SO) 3.4, Catalyze Improvement of Social and Health Services in Targeted Areas, is directed to Georgia's health and social services sector that is still precarious eleven years after independence. Poverty levels remain disturbingly high, caused by high unemployment and low wages for those who do have employment. Income inequality has become alarming, with a tiny minority enjoying lavish lifestyles, while the great majority barely survives. Nearly half of all formal employment is in the state sector and all state salaries, when paid, are significantly below the subsistence level. This fuels rampant corruption. Even if the state budget were fully funded, it would still be inadequate to meet minimum social and health needs. Pensions are equivalent to less than \$7.00 per month. Schools and health facilities are not maintained. Roads deteriorate and the imminent collapse of bridges threatens to cut off whole rural communities from markets. While life expectancy is not dropping precipitously (unlike in Russia and Ukraine) and the spread of vaccine-preventable diseases has been slowed, there are declines in some important health indicators. There is a noticeable rise in maternal and child mortality and in the rate of tuberculosis infection. Georgia has the highest induced abortion rate in the region. The rate of HIV/AIDS infection is low, but economic stagnation leads many to work abroad, while others turn to injected drug use in their hopelessness. These risk indicators suggest that HIV/AIDS could quickly become a significant threat. The high rate of abortion is a serious health threat to women. Finally, heavy reliance on informal payments hinders the effective use of health care resources.

B. Problem Analysis

Life for the vast majority of Georgians is significantly worse than it was before independence. Basic needs at the community level are not being met and it is unlikely that there will be any significant funding available from the central government during the timeframe of this strategy. Lack of progress in providing these needed services will serve only as a further brake on the economic and democratic development of Georgia, as people become more impoverished and more disheartened. One of the main elements currently sustaining social and political stability in Georgia now is the memory of the costs of violent conflict immediately after independence. As time passes, a new generation will emerge that does not share that memory.

Communities mobilizing resources to meet their own needs: These needs include both economic and social needs. Agriculture is the backbone of the economy, yet agricultural production is constrained through collapsed irrigation systems and difficult access to market centers. Parents often keep their children at home in the winter rather than send them to gutted buildings with cold wind howling through smashed windows. Community-based organizations (CBOs) can successfully lobby local governments to provide resources and cut through red tape. They also can convince local businessmen that they can be trusted with contributions. Even poor communities can meet an increasing percentage of community contribution. Community mobilization activities build trust among community members and also between citizens and government. Community groups must raise local contributions to implement projects. This effort includes contributions from the local government. Interaction with local officials

USAID/CAUCASUS-GEORGIA SO 3.4 RESULTS FRAMEWORK



Shared and Linked IR with SO # 2.31.3

increases local government transparency and sheds more light on municipal budgets, making corruption more difficult.

Employment: People need jobs. Most people will not become entrepreneurs and will need to work for a private business. Formal employment opportunities are not increasing at a rate sufficient to meet the need for productive employment for people in their prime earning years. Jobs can be most quickly created in the short-term through public works projects that are economically and financially viable. Such projects inculcate core values, habits and procedures, while they assist in maintaining social stability.

Health Care: Health care suffers from inadequate facilities and ill-trained staff. Communities are willing to contribute significant resources to address needs that they themselves have selected. Targeted early intervention, funded primarily by USAID, was instrumental in slowing the spread of vaccine-preventable diseases. Now Georgia faces increasing rates of tuberculosis and the emerging threat of HIV/AIDS. Inadequate antenatal care is causing a rise in maternal/infant mortality, while Georgian women seek repeat abortions as the birth control method of choice. Significant sums of money are spent by Georgians in under-the-table payments for health care, which does not help to develop the sector by encouraging infrastructure, equipment, and professional training investment.

The Ministry of Labor, Health, and Social Protection (MOLHS) has proven to be a reliable partner in past USAID-funded health activities. Georgian health professionals are receptive to new ideas. There are windows of opportunity to make the current system more efficient by instituting health policy/financing reforms in league with government, citizens, and communities, and to pilot community health funds to pool risks and to formalize individual health care expenditures.

Corruption in the health sector of Georgia is a major challenge and stems in large measure from the Soviet-style health systems that provided few financial and non-financial incentives to discourage corrupt practices. As revenues have declined, health expenditures have also fallen, resulting in underpaid or unpaid medical staffs and inadequate medical equipment, drugs, and supplies.

These conditions have created a corruption-prone environment. Petty corruption is the most common form of corruption in the health sector and affects the largest number of people. The poor suffer the most from health sector corruption because they represent the majority of people paying under-the-table. Providers continuously demand illegal payments from the patients, which create financial barriers for the poor. The amount paid represents a significant portion of the income of those already living in poverty. The inability to purchase health care often translates into death, disease, pain and disability, resulting in reduced productivity of the labor force and erosion of citizens' buy-in to democratic processes and ideals.

Similarly, grand corruption takes many forms. Examples include theft, fraud in the procurement of pharmaceuticals, equipment and supplies for hospitals, misallocation of resources for the health sector, lack of transparent decision-making processes, and insufficient or inaccurate data collection systems.

C. Development Hypothesis and Rationale

Passivity and lack of trust at the local level are factors in many of the most urgent problems faced by Georgia today. The inability to trust others outside of an immediate circle of friends and family impedes the business environment, disrupts the democratic process, and erodes the normal functioning of government services. In contrast, mobilized communities show an increase in mutual trust among community members. By catalyzing change in the social and health sectors at the community level, social stability will be enhanced, and key values can be promoted that will assist positive change in the economic and political spheres.

D. Critical Assumptions

- Economic growth and tax receipts will not increase to the point where there can be meaningful central government financing of key social and health needs;
- Local government will continue to have limited capacity;
- A minimal level of stability will exist in order to implement community-based activities throughout Georgia (excluding those areas controlled by separatists); and
- There will be continued support for SO activities from the MOLHS.

E. Progress to Date (1999 – 2003)

The Georgia Community Mobilization Initiative (GCMi) is the central activity currently being implemented. This activity has three components: Community mobilization over time culminating in a series of micro-projects with increasing levels of community contribution, NGO-led social service provision projects, and a Social Policy Initiative Group. Over 660 communities were mobilized in the first three years of the current Country Strategy. These communities made contributions equivalent to nearly \$2 million towards the micro-projects that they implemented. Assessments have shown increased trust and hope within mobilized communities and greater initiative and confidence in taking on projects on their own. GCMi maintained a significant presence in areas with heavy concentrations of ethnic and religious minority groups (Armenian, Muslim-Azeri, and Muslim-Georgian).

The Georgia Assistance Initiative (GAI) was active throughout the strategy period and began the process of transitioning Georgian communities from humanitarian assistance by implementing social infrastructure, health, and income generation activities through community-based methodologies. The GAI also served as a response mechanism to react to crises. It was instrumental in mobilizing international donor support to reduce the affects of a significant drought in 2000. Micro-finance institutions supported have reached operational sustainability and continue to operate without USAID support. The nutritional needs of 5,000 elderly persons were supplemented on a daily basis. Two youth programs were implemented throughout the strategy period that aimed at providing psycho-social services to conflict-affected youth. These programs also operated in the separatist controlled areas of Georgia and fostered contact between otherwise isolated and separated ethnic groups.

The Georgia Winter Heating Assistance Program provided critical support to vulnerable people while simultaneously helping to maintain social stability and supporting energy

sector reforms. Over 180,000 households and 560 socially critical institutions were assisted.

Major health interventions included five health partnerships concentrating on primary health care, women's health, health management, infection control, and a safe blood supply. These partnerships mobilized significant resources from US-based partners and helped to establish centers of excellence that work in close cooperation with the programs of other donors, such as the World Bank. Reproductive health programs included a major CDC-conducted survey, technical training, and communications and social marketing campaigns. These programs increased knowledge of modern contraceptive techniques. The final evaluation survey for one program in Tbilisi found that the percentage of married women in Tbilisi aware of the USAID program experiencing abortion to be reduced. The Georgian Safe Motherhood Initiative, in addition to raising the number of women seeking antenatal care, developed new treatment guidelines that are already credited by doctors with saving lives. The Health Information System activity has increased the ability of health care providers in one target region to better predict outbreaks of childhood communicable diseases. Products developed by the Health Information System activity have been approved for use country-wide. An innovative STI/HIV program targeted at high-risk groups in Tbilisi and Batumi is now underway.

Transition from SO 3.1 to SO 3.4: SO 3.1 was originally conceived as transitional in nature. Communities, although just emerging from a recent wave of crises, were already expressing a desire to move beyond humanitarian assistance. Starting from a base of mostly humanitarian programs in 2000, the portfolio in 2003 now has only one remaining humanitarian program. As health programs -- as well as USAID's relationship with the reform-minded MOLHS -- have matured, it is considered possible to achieve progress at the Intermediate Result (IR) level in the health sector. Progress in preparing communities to address problems on their own is evaluated as making possible the reduction of the prominence of crisis response from the IR level to the sub-IR level. The emphasis within SO 3.4 will continue to be on enabling communities to meet their basic needs, but there will also be more cooperative work between CBOs to solve problems by involving regional and sectoral clusters in problem identification and resolution.

F. Program Approach

1. Expected Results and Illustrative Activities

SO 3.4: Catalyze Improvement of Social and Health Services in Targeted Areas.

- People above poverty line reported by Georgia Department of Statistics rises in targeted areas; and
- The number of communities improving a service with their own resources rises.

An E&E bureau team will work with the Mission to refine these SO-level accomplishment statements.

Although improvement of these vital services is important, even more essential is that Georgians themselves make these improvements in a sustainable fashion. Funding will not be available to cover all areas of Georgia, so these activities will be concentrated in targeted areas. The "area" to be targeted can have either a geographic meaning and/or (especially for health activities) a sectoral meaning.

Two IRs will accomplish SO 3.4:

IR 3.4.1: Communities Meet Basic Needs. Communities will be mobilized to meet their own needs by increasing their capacity to deliver services, by fostering local economic development, and by responding to crises and other urgent needs. Issue-driven action originated by CBOs acting together to address community identified issues is included in this IR. Activities will seek the maximum contribution and involvement of local governments and business. Education will be addressed through the community mobilization process. Communities will continue to be linked with the World Bank education project, which funds national-level education reform activities. Employment is one of the most important basic needs. In addition to linking communities with credit opportunities to build employment in the private sector, this IR will include a targeted public works program. Community mobilization activities build trust among community members and also between citizens and local officials. Community groups must raise local contributions to implement projects, including contributions from local government. This interaction helps to increase local government transparency and sheds more light on local budgets, which makes corruption more difficult. Small-scale crises will be responded to at the community level predominantly using local NGOs.

Illustrative Activities:

- Community mobilization;
- Targeted public works program;
- Youth; and
- A residual feeding kitchen program.

IR 3.4.2: Prevention of Disease and Access to Quality Health Care Improved. Taking advantage of a supportive Ministry, improved clinical effectiveness will be fostered through sponsoring demonstration programs that can become national models and be replicated nationwide. Economic efficiency will be fostered, initially at the clinic and community level, in order to place health care providers on a business footing, to support accountability and transparency in the Health Care Financing System, and to reduce the share of under-the-table payments within the system. Support will be provided to local primary health care financing pilots (*e.g.*, pre-paid “polyclinic” and community-based arrangements) within the framework of the Georgia National Health Strategy, to allow for replication. This support will be complemented by modest assistance to national level health entities to foster better provider standards, quality control, and competition, with an emphasis on creating an informed health consumer. Infectious disease control and prevention will be strengthened to help ensure that Georgian economic development is not impeded by an unhealthy workforce. The health program will support community-based health care financing mechanisms that collect fixed premium payments and pay providers a fixed capitation fee for delivering primary health care services outside of the current “basic benefits package.”

Illustrative Activities:

- Health partnerships;
- TB interventions;
- Health Information Systems;
- Women’s health;
- Vaccination programs;
- Health care financing;

- Technical assistance in the areas of national health accounts and legislative/regulatory reform;
- IEC campaigns;
- patient advocacy; and
- Risk-pooling pilots.

Hospitals, especially the new World Bank-funded Gudashauri Hospital and Children's Central Republican Hospital, will play an important role in the development of clinical care training, business development and management models, and Health Care Financing models.

2. Performance Indicators

IR 3.4.1: Communities Meet Basic Needs.

Illustrative indicators: Number of community projects completed, number of direct beneficiaries, number of community groups organized, percentage and value of community contribution, the number of loans received within communities, the number of jobs created or sustained, and the proportion of individuals in need during crisis assisted by USAID emergency relief programs. Rising levels of local government contributions is an anti-corruption indicator as it serves as a proxy for rising trust and transparency.

IR 3.4.2: Prevention of Disease and Access to Quality Health Care Improved

Illustrative Indicators: Overall immunization rates, number of targeted health care facilities meeting selected international standards, decrease in abortion rates in selected regions, number of pregnant women attending all four government-provided antenatal consultations, TB incidence per 100,000 and the number of individuals receiving voluntary counseling for testing for HIV/AIDS.

Discussion of Anti-Corruption Activities

Illustrative anti-corruption activities in the health sector would include the following:

- Support community-based health care financing mechanisms to collect fixed premium payments and pay providers a fixed amount per person for delivering primary health care services outside the current "basic benefits package";
- Establish mechanisms to more closely monitor disbursement of funds, cost of delivery of services contracted, or other mechanisms to flag possible fraud;
- Post services fees in health facilities so that patients know the pricing structure before services are rendered;
- Establish a system for health facilities administration for internal control and management of operations and financial reporting including control procedures over the receipt, storage and use of drug and medical supply inventories and collection, recording and accounting of cash for user fees; and
- Inform the public through training, media, and public service announcements about how financing of health care occurs, their entitlements to health care, basic functions of an insurance system, and the range of possibilities for payment sources in a fee-for-service environment.

G. Linkages to Other SOs and Cross-Cutting Issues

- Social and ethnic stability enhanced through community mobilization assists in the achievement of other SOs, while the country-wide network of CBOs created through community mobilization creates entry-points into communities for the activities of other SOs.
- One sub-IR of SO 3.4, “Increased capacities to deliver social services identified by communities,” is linked closely to the SO 2.31 sub-IR, “More effective citizen participation in community development.” The results framework for the Mission shows this relationship by a dotted line encompassing both sub-IRs. While these sub-IRs focus on different results (increased capacities as compared with more effective citizen participation), they share some components in common that can provide positive synergies, but also require close coordination.
- One sub-IR of SO 3.4, “Foster local economic development,” is linked closely to SO 1.31. SO 3.4 focuses on creating a positive local environment for productive firms to operate within.
- Corruption: Combating corruption requires the reestablishment of trust at the local level and through transparency in government operations. These are two of the results routinely achieved through community mobilization.
- Coordination for Local Impact: Community mobilization activities will be designed to ensure maximum flexibility to respond to opportunities created by activities under other SOs.
- Youth: The majority of mobilized communities select education as their priority, thereby directly assisting the youth of these communities. Additionally, youth programs addressing the psycho-social needs of conflict-affected youth, and encouraging ethnic reconciliation, address the needs of youth at the age at which they are most vulnerable, adolescence.
- Conflict: Youth and limited humanitarian assistance programs (and potentially community mobilization in Tskhinvali) assist in confidence building between the conflicting sides. SO 3.4 ensures that areas populated by ethnic minorities receive appropriate levels of assistance, helping to increase contacts between these often remote regions and the rest of Georgia.

H. Resources Requested and End Date

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Proposed End Date: September, 2010.

I. Sustainability

Long-term sustainability in the health sector depends on the formal privatization of services using various insurance modalities for the majority of beneficiaries. Lasting progress in community development will coincide with the assumption of basic tax authorities and responsibilities by elected local councils. Sustainable educational reform will require a stable local tax-base and revised authority structures between the national Ministry of Education and local school boards.

J. Other Donor Programs and Impact on SO Results

- Georgia Social Investment Fund II (World Bank-funded): This five-year, \$30 million program concentrates on rehabilitating social infrastructure identified through the community mobilization process. The World Bank and USAID have formed a partnership, under which USAID-funded activities will provide most of the community mobilization for GSIF II. Downstream infrastructure loans from GSIF will allow USAID implementers to greatly leverage their micro-project assistance by linking supported communities with significant additional resources.
- World Bank Education Loan: This major program will provide much of the funding needed for educational reform in Georgia. The World Bank considers that USAID community mobilization activities cover many gaps in loan-funded activities.
- World Bank-funded Gudashauri Hospital: This hospital provides an excellent opportunity to pilot clinical effectiveness training as well as training in improved economic efficiency.
- World Bank, EC, and DFID-funded Primary Health Care: These coordinated programs have three basic components, renovation of rural health clinics, clinical equipment, and training. Agreements have been reached to coordinate and cooperate with USAID-sponsored activities.
- Global Fund Grant for HIV/AIDS prevention in Georgia: Georgia has recently been awarded \$12 million from the Global Fund. USAID has provided technical assistance to the MOLHS proposal, which complement USAID-funded HIV/AIDS programs in Georgia.
- Baku-Tbilisi-Ceyhan (BTC) Community Investment Program (CIP) implements community mobilization programs along the BTC pipeline route on the GCMI model and in coordination with the GCMI partners and USAID-supported micro-finance institutions.

K. Activities Not Supported

Although some, targeted, assistance to the MOLHS will likely continue through the Mission training program and other mechanisms, major technical assistance to GoG ministries on social and health issues will not be the emphasis of this strategy. The Mission's decision to proceed with caution into the health and education sectors reflects the broadly embraced perception among donors that national-level GoG officials are not yet prepared to implement major changes in the social sector administration -- no matter how collapsed their infrastructure may be.

A critical adverse factor in health is that it is considered to be the most corruption-prone sector with little grasp of how to replace a Soviet-style administration with one based on self-sustaining insurance principles. The Mission's health care finance initiative will analyze the health finance environment and generate options that are viable and less dependent on impoverished state coffers. During the next two years, while Parliamentary and Presidential elections provide indicators of the mid-term prognosis, USAID will move forward with approaches to health care at the community level that may be replicated once reformist leaders return to positions of national authority. The reader is directed to Annex F, Possible Program in Health Care Financing: Constraints and Priorities, as well as Annex G, Situational Analysis of Health Sector Policy and Financing in Georgia.

National authorities retain monolithic control over Georgia's educational system that has not changed since independence. The Ministry of Education not only controls the curriculum, policy direction, and teacher training institutions for Georgia but also dictates local personnel decisions, imposes an annual budget for each school, and requires local councils to fund the program without debate or recourse. This heavy-handed approach to what are essentially local matters does not bode well for a massive reformist agenda at this time. Fortunately, the World Bank and Georgia have committed themselves to a major, long-term project to revise the curriculum. As a late arrival to the education debate, the Mission believes USAID's scarce funds can best be focused on ensuring a comprehensive approach to civics at all grade levels and by mobilizing communities to hold teachers and school principals accountable to elected local council members for the stewardship of local monies. Annex I, Primary and Secondary Education in Georgia, provides a snapshot of the key issues in Georgia's educational system.

Continued economic problems, corruption, and national government inefficiency make it unlikely that sufficient funds will become available to fund social and health services adequately from the central government. In fact, these serious managerial short-comings argue that the GoG has limited absorptive capacity for major direct government-to-government assistance programs at this time.

Strategic Objective 4.1 Special Initiatives

This SO is comprised of three programmatic areas that are of critical importance to the overall strategy. These three activities are designated as Special Initiatives (SIs):

elections assistance, anti-trafficking in persons, and anti-corruption. The rationale for targeting these three areas was discussed earlier in Part II.B.2. USAID does not intend to create new administrative units to manage these three SIs. Designation of responsible management units is discussed below under each SI.

1. Elections Assistance 4.1.1.

A. The Problem and the Context

The 2003 Parliamentary elections, and 2005 Presidential elections, hold real promise for Georgia to sustain itself as a democracy. The outcome of elections as a free and fair process will play a pivotal role in either fulfilling that promise or categorizing Georgia as a “failed state”. The Parliamentary elections may well foretell Georgia’s success or failure in making the transformation from a troubled post-Soviet republic to a viable nation state: one that is able to effectively respond to citizens’ needs, and rooted in sound democratic principles. These elections will either usher in a group of reformers who are concerned about Georgia’s future and desire to minimize pervasive corruption or allow unfettered growth of leaders who not only turn a blind eye to these corrosive elements, but also actually aid and abet them.

Reform measures have thus far established only a tenuous hold in Georgia. Peaceful, fair Parliamentary elections represent a critical first step to the post-Shevardnadze era. The party or coalition that controls Parliament will dictate the legislative agenda. They might have enough clout to either reverse or accelerate key reforms. Electoral winners may even garner enough seats in 2003 to amend the Constitution.

Georgia stands at a crossroads with its citizenry. Each day people grow increasingly frustrated at stalled reforms and empty promises. Citizens have all but lost confidence in their government. In a recent poll conducted throughout the country, fewer than ten percent of respondents voiced faith in either the executive or legislative branches of government. Many youth, Georgia’s future, refuse to even vote, citing stolen votes and politicians who fail to fulfill their promises. Too long they have seen their country torn asunder by those in power who pay only lip-service to ending the scourge of corruption, economic stagnation, and political stalemate that has paralyzed Georgia’s transition in recent years.

USAID elections assistance also is seen as a critical component of our near-term conflict mitigation strategy. Conducted without sophistication and sensitivity, the Parliamentary and Presidential elections risk simply feeding societal tensions. Many Georgians still yearn for the patronizing security of the former Soviet Union, see reformers as the enemy, and could well bring their resistance to change to the streets if measures for conflict mitigation and violence avoidance are not vigorously pursued. Accordingly, all key USAID elections assistance providers and partners will be trained in conflict mitigation technologies, and great care will be taken to ensure that, above all, we “do no harm.” Recognizing the critical nature of these elections, the U.S. Embassy has declared them one of the top three priorities of USG assistance to Georgia.

B. Planned Activities

The elections assistance Special Initiative under SO 4.1 addresses four critical areas: credible election administration; assisting political parties to represent citizen concerns and interests; educating the electorate to actively participate in the election process; and monitoring elections. Several critical measures must be launched as key underpinnings for democratic elections. Activities in three key areas will be supported: election administration, political party development, and voter education.

1. Election Administration: Several important elections administrative processes must be in place in order to achieve credible electoral processes:

- Trained and Credentialed Election Administration Officials;
- Centralized, Computerized Voter Registry;
- Legislative Reform; and
- Voter Identification System.

2. Election Monitoring: Several initiatives will be undertaken, including:

- Training and credentialing election monitors;
- Training judges in the election code and violations procedures;
- Parallel vote tabulation;
- Media watchdogs;
- Timely publicizing of election results by precinct; and
- High-level political delegations pressuring GoG for election reforms.

3. Political Party Development: Political parties must represent the interests of citizens, and be based on issues rather than personalities. Illustrative activities include:

- Assisting political parties to develop platforms addressing citizen concerns; and
- Training independent candidates, particularly women and youth, to effectively run for office.

4. Voter Education: The electorate must understand key issues, insist that parties represent their concerns, and monitor the election process. Illustrative activities include:

- Get-Out-the-Vote Campaigns, targeted to the general population, women, and youth;
- Voter education on issues, candidates, and voting procedures; and
- Public service announcements and neighborhood and town meetings.

C. Expected Results and Timeframe for Achievement

The results framework found in Annex L illustrates the objective and Intermediate Results (IRs) of the elections assistance Special Initiative. Performance indicators for the IRs have been identified. USAID believes that, if these election assistance measures are taken, voter confidence in elections will increase. In addition, five specific benchmarks also will be achieved:

- Georgia's first centralized, computerized voter lists will be completed and utilized for both Parliamentary and Presidential elections, and maintained for the 2007 Parliamentary elections;
- Legislative reform will improve the existing Unified Election Code, introducing additional anti-fraud measures;
- Domestic monitors will improve their technical efforts, and complaints will be successfully lodged in court; and
- Judges will understand the complaint process and impartially adjudicate complaints.

The results are expected to be achieved during the first 18 months of the strategy -- through the Presidential election in the spring of 2005.

D. Resources Requested

The estimated amount per year needed to achieve results is as follows:

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The End Date shall be September, 2005. From FY 2006 onwards, any additional support for elections, such as the projected municipal elections in 2006 and another Parliamentary election in 2007, will be funded as appropriate under SO 2.31.

E. Management of the Elections Assistance Special Initiative (SI)

The Democracy and Governance Office will manage this Strategic Initiative. A USDH Democracy and Governance Officer, supported by USPSC and FSN specialists, will form the Democracy and Governance core team. Please see the Elections Assistance framework under Annex L.

2. Anti-Trafficking in Persons 4.1.2.

A. The Problem and the Context

This Special Initiative's objective is to prevent the recruitment of persons living in Georgia from being trafficked for foreign exploitation. Since independence, Georgia has lost over 20 percent of its population who voluntarily left in the wake of deteriorating employment opportunities at home and a desire to improve their economic situation. While most of this migration abroad has been perfectly legitimate, some reportedly has resulted in a fraudulent abuse of human rights and values. Traffickers inside and outside Georgia have taken advantage of this situation by deceiving vulnerable young women to relocate to countries demanding cheap, undocumented labor and commercial sex workers. They also have exploited men and children who honestly seek better lives abroad. The desperate economic situation in the country, coupled with a total collapse of infrastructure and social safety nets, has lured unsuspecting victims into these traffickers' traps. If they are ever able to return, their families and friends likely shun them. Meanwhile, while traffickers in Georgia and their collaborators overseas collect revenues from this form of modern-day slavery, no charges have been brought against the alleged perpetrators of these heinous acts, since -- until the summer of 2003 -- trafficking was not classified as a

crime under Georgia's Criminal Code.

No reliable data exist in Georgia to accurately define the scope and magnitude of the problem. Most anecdotal information indicates that the problem has not yet reached the proportions found in countries such as Ukraine and Russia, where thousands of women are trafficked each year. However, these same sources claim that the problem is growing in Georgia. The International Organization for Migration (IOM) has recently conducted two studies that interviewed irregular migrants returning to Georgia. The most recent study interviewed 270 irregular migrants. Their data illustrate a profile of trafficked victims in Georgia²¹: 87 percent female (55 percent aged 21-30; 30 percent aged 31-40; 50 percent single; 49 percent with children; 33 percent from Tbilisi; 28 percent from Shida Kartli/Mtskheta; 24 percent from Kakheti; 41 percent secondary school education; 29 percent vocational school education; 17 percent university education). Although the majority of victims are women, men and children also fall prey to traffickers' ruses. Thus, USAID/Caucasus-Georgia will address both genders in its anti-trafficking Special Initiative.

Three key legal and regulatory references underscore the urgency of this activity:

DOS' Annual Report on Trafficking in Persons: The report categorized Georgia as a Tier 3 country not in compliance with minimum standards and given 12 months to take corrective measures or risk jeopardizing USG foreign assistance. (During the 90-day "grace period", Georgia made enough progress to warrant a return to Tier II.); The Victims of Trafficking and Violence Protection Act of 2000 requires the DOS to submit to Congress each year a list of countries of origin, transit, or destination for victims of "severe forms of trafficking"; and Trafficking Victims Protection Act (Division "A" of Public Law 106-386): Beginning in FY 2004, countries listed by the DOS as failing to make significant efforts to meet minimum standards to end severe forms of trafficking are subject to cut off of non-trade, non-humanitarian aid, unless granted a waiver for U.S. national security reasons.

The Timeframe: While the problem of trafficking in Georgia warrants special and urgent consideration, there is a more immediate, political rationale for Georgia to discourage trafficking. If Georgia backslides in its renewed commitment to anti-trafficking, it risks the disfavor of the USG and potentially the loss of at least a good portion of its foreign aid according to existing U.S. legislation. Such measures therefore underscore the urgency of this Special Initiative: Georgia can ill afford to lose any of its future foreign assistance. The Mission also would prefer to address the problem while it is still manageable. Although all data indicate that this problem has not yet reached epidemic proportions, the continuing downward spiral of Georgia's economy continues to demoralize young people who seek gainful economic opportunities. They will be lured into the traffickers' traps unless they are warned, and until their country can offer them a brighter future. Launching the anti-trafficking SI at this time will no doubt result in these vulnerable persons having a better understanding of the dangers facing them, and hopefully deter their illicit travel.

²¹ International Organization for Migration. "Hardship Abroad or Hunger at Home: A Study of Irregular Migration from Georgia." Tbilisi: September, 2001.

B. Planned Activities

Approach: The USG has developed a three-pronged approach to the problem of trafficking in persons: (1) prevention of the problem through improving economic opportunities and warning potential victims of the risks at hand; (2) protecting victims through crisis centers, shelters, and other medical and psychological measures; and (3) prosecuting traffickers. USAID/Caucasus-Georgia's Special Initiative will focus on the first approach: preventing victims from being trafficked.

Illustrative Activities: This will be the first time that an anti-trafficking in persons (TIP) program will be implemented by the Mission. The program will begin with a well-designed research component geared to better understand the structure of the problem, followed by an inventory of all anti-TIP programs operating in Georgia. The results of these first two steps (research and inventory) will determine the specific activities to be undertaken. These anti-TIP activities will be integrated into existing USAID programs implemented by Eurasia Foundation (Georgia), ABA/CEELI, GCMI, IREX, and others.

i. Research - Examining the Nature of the Problem: A critical first step is to better understand the nature of the problem.²² Information that better identifies persons at risk of being trafficked, their socio-economic profile, demographic information, and geographic information will prove useful in targeting assistance. Links between trafficking and domestic violence also can be explored at this time.²³

ii. Inventory of Existing Anti-TIP Activities in Georgia: Second, an inventory of existing activities, funding source, effect, and lessons learned also is crucial in order to avoid possible duplication of efforts. Such an inventory can also help to set forth "best practices" for Georgia, including cost of interventions, number of recipients, and potential gaps in assistance.

iii. Integrating Activities into USAID's Current Development Portfolio: Following the initial research and inventory, activities can be designed that will effectively address the problem in a targeted and meaningful way. Many of these activities can be integrated into existing programs at little to no additional cost. Three potential activities hold immediate promise for synergies:

- **Economic Opportunities:** Potential activities include public awareness and education of potential victims, and targeting assistance (skills-oriented vocational training, etc.) to those at greatest risk to become victims of traffickers in high-risk geographical areas;
- **Public Awareness:** Educating the public about the nature of trafficking, and warning them of these dangers, will help avert trafficking. Supporting hotlines and/or crisis centers in major targeted cities would enable potential victims to learn details about questionable job opportunities. Posters, leaflets, public service announcements, and

²² Reliable figures on the scope of the problem, *i.e.*, how many persons have been illegally trafficked, are extremely difficult to accurately ascertain. Traffickers often are violent criminals who threaten both victims and their families if they speak out. Returning victims often are ostracized if they dare to disclose the realities of their lives abroad. Accurate data collection proves extremely problematic in this area.

²³ In Ukraine, between 25 to 30 percent of trafficked victims come from homes where they were abused.

other means of public education can curb this problem. Local governments also can take responsibility for spreading the word about these threats. Potential partner organizations to join this effort include GCMI, Urban Institute, IREX, Eurasia, and the STI/HIV program; and

- **Public Policy and Legislation:** Georgia must take this issue seriously and pass meaningful legislation to prosecute traffickers. Potential partners include ABA/CEELI.

C. Expected Results

Three intermediate results form the basis of our anti-TIP strategy:

- Provide economic opportunities to those at risk of being trafficked
- Raise public awareness and warn potential victims
- Assist the GoG to establish and enforce a new statute to prosecute traffickers

Specific results related to the three IRs noted above are:

- 25 percent of targeted individuals will have access to opportunities that can improve their economic livelihoods
- 75 percent of individuals in target groups in risk-prone areas are aware of the dangers of trafficking
- Legislative and regulatory measures based on international norms are developed, enacted, and implemented by GoG

These targets and indicators will be carefully examined and developed during the initial phases of the program to assess their relevance and accuracy for measuring progress.

D. Management of the Anti-TIP Special Initiative (SI)

To ensure optimal coordination with all USG entities and other donors working on this issue in Georgia, this program will be overseen by USAID's Program and Project Support Office and managed by USAID's Democracy and Governance office with assistance from the Embassy's Consular section. During Year-3 of the Special Initiative, a mid-term evaluation of the TIP program will be conducted to assess progress. Mid-course corrections can be made at that time. At the end of the Year-5, a final evaluation will be completed to assess results, lessons learned, and best practices.

E. Resources Requested

The End Date shall be September, 2008. An estimated - - - - - is requested for the anti-TIP Special Initiative:

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Please see the anti-TIP framework under Annex L.

3. Anti-Corruption 4.1.3.

A. The Problem and the Context

Pervasive corruption in Georgia is an endemic “way of doing business.” It permeates all levels of government and affects all segments of society. Corruption in Georgia is built on a clan-based system of survival, which evolved and was refined over the last several centuries. It continued and became more sophisticated under the Soviet regime. It is now flourishing due to an influx of cash from smuggling, tax evasion, and bribe-taking, non-transparent transactions, lack of accountability and enforcement mechanisms, and a lack of effective checks to prevent corrupt practices. Georgian citizens themselves are most affected by the current status quo of rampant and systemic corruption. A USAID implementing partner put it well: “Individual Georgians themselves must embrace a code of anti-corruption. That’s where the real change needs to happen.”

Since the fall of the Soviet Union, corruption has emerged as a key development concern constraining further development of Georgia. No sector supported by USAID programming is left untouched by corruption. Corruption has been a significant and persistent impediment not only to foreign investment but also to development in general. Its pervasive nature and high visibility have stunted economic growth, eroded the educational system and social services, destabilized the energy sector, and seriously undermined the credibility of the government, its reforms and the rule of law in general.

The Present State of Corruption in Georgia: The perception, visibility and systemic nature of corruption in Georgia are important factors in designing anti-corruption activities. However, the Donor Standards in Anti-Corruption²⁴ report notes that “...for all of the incremental successes and promising processes that donors have underwritten and witnessed in the last decade, in the end there appears to have been little or no tangible reduction of corruption. Indeed, some observers attest to a worsening of corruption and, perhaps even more seriously, a deepening cynicism among the public at large about the prospects for meaningful change.”

Corruption may be grouped into two basic categories: petty corruption and grand corruption. Petty corruption spans all sectors of Georgian society and is experienced in everyday life in Georgia. Petty corruption can be exemplified by payments for officially-free basic social services, bribes for gas and electricity company collectors so service is not suspended or is disconnected, continual traffic police stops, customs officers’ “facilitation fees”, and tax officials’ hectoring -- in other words, essentially the standard menu of corrupt practices experienced throughout the former Soviet Union but perhaps with a special blatancy, pervasiveness, and imaginativeness. Most drivers, and those individuals subject to customs and tax duties, simply pay the bribes because it is easier to make the problem go away rather than pursue official routes which may require that a higher bribe be paid.

²⁴ Hensen, Greg, Case Writer, Donor Standards in Anti-Corruption (DSACP) “The Struggle against Negative Occurrences: Experience with Explicit and Implicit Anti-Corruption Efforts in Georgia,” September 2002.

Grand corruption is found at the higher levels of Georgian government. Examples include unsolicited gifts from those wanting favorable treatment, wholesale usurpation of public assets for private gain, distortion or elimination of competitive economic systems to favor the select few, and pressure from well-connected colleagues and higher officials. Threats -- and acts -- of physical harm, including murder are relatively commonplace and central to the corruption system. Tolerance through inaction in the face of massive smuggling of many primary commodities (*e.g.*, petroleum (“white oil”) products, cigarettes, flour and sugar) is also essentially grand corruption.

In 2002, Transparency International’s Corruption Perception Index ranked Georgia 85th of 102 countries. Georgia scored 2.4 out of 10 in a ranking system where 10 is highly “clean” and 0 is highly corrupt. A 1998 survey of public perception of dishonesty conducted by USAID and the World Bank found that public suspicions of corruption were wide-ranging. Corruption is increasing as elites regain their footing after the political and economic crises of the nineties, and as a higher level of economic activity creates new targets for “rent-seeking”.

The high visibility of corruption in daily life, the lack of criminal convictions despite many allegations of corruption, and the ostentatious shows of wealth among political and business leaders have bred distrust among the public and resignation about their inability to stem the tide of systemic corruption. Most alarmingly, the corrosive effect of corruption on the mindset and self-image of Georgia’s citizens cannot be underemphasized. The sense of powerlessness in the face of corruption, together with the absence of broad-based economic growth which could alleviate poverty, helps produce a profound sense of fatalism and negativity among Georgians, which becomes self-actualizing in terms of the nation’s growth and development.

Why Highlight Corruption in the Country Strategy: The impact of corruption, and the necessity to tackle it head-on, pervades virtually the entire USAID program. It is also a Cross-Cutting Issue adversely affecting the realization of democracy and governance, social transition, energy and economic growth. Left unchecked, corruption in Georgia has the potential to hamper U.S. interests to promote regional stability, the rule of law, and integration of Georgia into the larger international community and global marketplace. Corruption acts as a “tax” on our investment in Georgia’s economic growth. It fosters poverty, destabilizes political processes, discourages job creation, and limits market access. The development of a friendly investment environment, a major goal of sustainable development, is not likely obtainable if the present scale of corruption in Georgia remains unchecked. Other U.S. interests such as reduction in terrorism and interdicting the flow of illicit drugs will be poorly served, if the criminality bred of corruption is not thwarted. Therefore, USAID/Caucasus-Georgia intends to integrate and implement anti-corruption measures systematically across the four “core” SOs.

B. Planned Activities

Throughout the USAID assistance portfolio, activities will be designed to raise the awareness of the costs of and opportunities for corruption in each sector. Greater emphasis will be placed on: prevention and enforcement efforts, increased transparency and accountability, identifying and fostering “islands of integrity” within each sector, fostering a transparent and accountable operating environment for public and private sector institutions, and identifying “champions” from both the public and private sectors.

The Mission will engage civil society, business and government in a non-adversarial partnership to take action to combat corruption.

USAID/Caucasus-Georgia will support the generation of effective and realizable demand for reform; Georgians themselves must take control of their destiny and lead the fight against corruption. To this end, USAID/Caucasus-Georgia and other donors will partner with those within Georgia both in the public and private sectors engaged in genuine anti-corruption efforts.

The proposed program of anti-corruption activities will be implemented at two levels:

1. Stand-Alone Anti-Corruption Activities (within the SI):

To reinforce Mission commitment to this area, USAID will implement stand-alone activities under this SI (in addition to SO-level activities), to elevate anti-corruption activities to a higher and more visible level within USAID/Caucasus-Georgia. These activities will support and underpin activities implemented under the SOs:

- Organize seminars and workshops as outreach mechanisms and forums such as films, brown bag lunch series, NGO briefings including the USAID IG fraud and corruption awareness workshops, etc. to disseminate new tools on anti-corruption activities;
- Conduct policy research and analysis through local organizations to improve understanding of the causes, patterns and costs of corruption prevalent in Georgia, and promote awareness of the results of surveys, reports and assessments with a view to decreasing tolerance for corruption and identifying pathways to change;²⁵
- Identify training needs, guide development of training plans and identify candidates that are potential champions for strengthening integrity systems and increasing transparency and accountability in State and civil society institutions;
- Implement specific anti-corruption activities through funding of small grants targeted for “quick response” activities, new entry points, and similar opportunities for combating corruption and promoting transparency and accountability that cannot be handled appropriately or effectively within the SOs; and
- Develop anti-corruption checklists for future RFAs and RFPs.

2. Anti-Corruption Activities at the SO Level:

Anti-corruption activities are built into the program of each SO. Because of the newness of this area these activities are illustrative at this stage. A detailed plan of anti-corruption initiatives will be developed by each SO based on an assessment of corruption in its sector applying the Europe & Eurasia Bureau’s anti-corruption strategy known by the acronym of “TAAPE” (Transparency, Accountability, Awareness, Prevention, and Enforcement). See Annex K for a brief note on applying the TAAPE methodology.

C. Expected Results

The anti-corruption SI anticipates the development of a strong Georgia public-private partnership to reduce corruption. It will increase awareness of the costs and opportunities for corruption, and promote transparency, accountability and integrity in government as

²⁵ To the maximum practicable extent, this research (and training) will be done through existing USAID contracts and agreements.

well as nongovernmental activities. As a result of weaving anti-corruption activities into each of the USAID programs/activities, we envision that citizens will demand constructive change from their government and that more transparent systems will be put in place and enforced. With these measures in place by 2008, we would hope to see Georgia move up the TI Index from its current 85th position.

Six results are expected over the strategy period:

- Increased awareness and understanding by Georgian society regarding the causes and costs of corruption, resulting from advocacy and lobbying for reforms;
- Civil society, business and government engaged in a non-adversarial partnership to address and combat the common problem of corruption;
- Local-level initiatives on anti-corruption efforts have become an impetus for change at the national level;
- Reformist policy makers are better able to gauge the specific costs of already-identified areas of corruption, and the tangible benefits of corrective measures;
- GoG effectively implementing its program on anti-corruption; and
- Significantly improved prosecution enforcement.

D. Resources Requested

The end date should be September, 2008. - - - - - is requested for the stand-alone anti-corruption Special Initiative.

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The End Date shall be September, 2008. In addition, the four “core” SOs will fund specific anti-corruption activities as integral parts of their respective programs.

During Country Strategy year-3, USAID/Caucasus-Georgia will undertake an assessment of the anti-corruption SI and make mid-course corrections as needed

E. Management of the Anti-Corruption Special Initiative (SI)

Most of the programmatic impetus and operational activity in USAID’s anti-corruption agenda will remain with the four “core” SOs, since this is where the bulk of Mission resources and attention reside. Each SO has been carefully reviewed to ensure that anti-corruption objectives are sufficiently integrated into the SO and its results framework.

This SI will be coordinated and managed by the Anti-Corruption Special Initiative Team comprising membership from all four “core” SO teams, RLA, and PPS. The anti-corruption team will be responsible for raising the profile of corruption and reinforcing emphasis on combating corruption and increasing transparency and accountability throughout the USAID assistance portfolio. The SI team will also be responsible for: designing and implementing discrete anti-corruption activities; functioning as USAID/Caucasus-Georgia’s focal point of the Mission’s anti-corruption expertise on combating corruption; ensuring that anti-corruption activities are incorporated into each SO; and coordinating anti-corruption activities with other USG agencies. The Regional Legal Advisor will chair the anti-corruption SI team and ensure day-to-day functioning of the activities.

The anti-corruption SI Team will:

- function as USAID/Caucasus-Georgia's focal point of the Mission's anti-corruption expertise to provide direction to the SOs on ensuring that anti-corruption activities/aspects are incorporated into each statement of work, pre-obligation checklist, work plan, conference, workshop, RFA, RFP and associated evaluation criteria;
- monitor anti-corruption activities and indicators across SOs and Cross-Cutting Issues and coordinate reporting requirements on anti-corruption activities;
- track innovative developments in anti-corruption activities; and
- coordinate anti-corruption activities with other USG agencies providing assistance in Georgia such as DOJ, U.S. Treasury, implementing partners, and other donors through meetings and workshops. As part of their duties, anti-corruption team members will dialogue with GoG principals plus donor and civil society representatives to share best practices, build trust, and establish strong relationships to counter corruption.

Please see the Anti-Corruption framework under Annex L.

Strategic Objective 4.2 Program Support

Strategic Objective 4.2's Program Support is comprised of three primary components that directly support the four "core" SOs and SO 4.1. The three components are: (1) participant training, (2) small grants assistance for activities of an innovative or pilot nature, and (3) program development and support functions. Training and grant components are expected to make demonstrable contributions to the achievement of results.

Participant Training

While an enabling environment for economic reform and a more democratic society has been gradually emerging at the national level, the benefits of these reforms have not trickled down to society as a whole. This predicament has left Georgians skeptical and suspicious of the positive impact these reforms can have on improving the overall well-being of the population, especially the poorer strata of society. Georgians need skills, values and knowledge on which democracy and free market economies are based, *e.g.*, the role competition and demand and supply forces play in free market economies; sound private business management and practices; the rights and responsibilities of citizens and groups in a democracy; and the role of elected local governments in promoting development.

Training supports all SOs to achieve this common objective. USAID supports a regional participant training program in the Caucasus. The Strategic Technical Assistance for Results with Training (START) program is implemented by World Learning, a U.S. firm. Participant training programs have been carried out in the United States, in-country, and in third countries as well. Various participant training programs that are critical for accomplishing the results under the strategy, but which are not unique to a given SO, are funded under SO 4.2's participant training mechanism.

Training will supplement technical assistance activities and equip host country leaders and professionals with the skills and knowledge needed to guide their country's transition to a free market economy and democratic governance.

Small Grants Assistance

The small grants assistance program complements the activities under the SOs that are innovative and pilot in nature. The small grants program is managed by a non-profit, grant-making organization that provides financial support to local organizations for programs promoting economic and democratic reforms in Georgia. Currently, a U.S. NGO, the Eurasia Foundation (EF), which has had a successful program in Georgia since 1995, implements this program. Since the EF has been working throughout the Caucasus, its experience and perspectives have demonstrated the value of these programs to achieve the results sought in this Country Strategy. As the Plan moves to consolidate gains made through various reforms at the macro level and to funnel them to society as a whole, our small grants assistance program will serve as a valuable component in fostering association-building and organizational development at the local and community levels. This activity will concentrate on targeted geographic areas and selected organizations that directly impact achievement. Illustrative activities key to the reform process are business development and education, management training, NGO advocacy, local government reform, NGO development, and rule-of-law. Pilot activities falling under SO 4.1's three

Special Initiatives (elections assistance, anti-trafficking-in-persons, and anti-corruption) may also receive funding under the small grants assistance program. The small grants program will bring synergistic benefits across the Mission's portfolio.

Program Development and Support (PD&S) Functions

The Mission will strengthen its program evaluation, assessment and review functions in support of program development and management. Design of new programs and activities, including program extensions with additional funding, will be based on (1) external evaluations, (2) critical, internal assessments of experience, and (3) "lessons learned" from past USAID support in the relevant areas. In addition, the following will also be funded under the PD&S element of SO 4.2: public education and information programs; supporting certain critically required positions providing services across the Country Strategy, and meeting certain administrative and operating costs directly related to program management and implementation (office space, logistics, staff development and management support).

Resources Requested and End Date

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SO 4.2 activities will continue as long as there is an ongoing Country Strategy for USAID/Caucasus-Georgia.

PART IV: RESOURCE REQUIREMENTS

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The Country Strategy narrative describes an alarming, long-term crisis in the social sector. Georgia's desperate situation is mirrored throughout the former Soviet Union and is not unusual. To resolve the administrative, financial, and policy issues common to the social sector, the GoG must re-assume its duty to guide the delivery of what are inherently public services: health, education, and welfare.

Resolution of Georgia's current deficit in social spending is clearly beyond USAID's manageable reach. However, certain activities in coordination with other donor programs

can lay the foundations on which sustainable national institutions can be built, once Georgian citizens and Georgian political leaders express the will to work together for the common good.

Donors concur that political will must first be assured before further major efforts at the national level can be effective. The results of the upcoming elections may confirm that Georgia once again is ready to take up serious national debate on reforms. Until that time, most donors to Georgia are focusing assistance resources on community-based initiatives to pilot systems that will later bear fruit in the form of a participatory citizenry more conversant with their rights and more demanding of their elected representatives.

The allocations proposed for the health and education sectors are higher than ever before. Nevertheless, they pale in comparison to the total need. As the Mission's mortgage lessens after the first two years of the Country Strategy, there will be more flexibility. Conversely, if OYB levels were higher, USAID could respond to opportunities sooner.

Strategic Objective 1.31: “Accelerated development and growth of private enterprise to create jobs” will deal with the overall development of the private sector. Principal activities will be demand-driven policy reform, improving competitiveness, promoting value-added agricultural products for domestic and export markets, strengthening trade and business associations and industry clusters, land privatization, and micro-finance.

Strategic Objective 1.51: “A more economically sound and environmentally sustainable energy system” will continue focusing on energy sector reforms, privatization of distribution systems, and supporting the rehabilitation/development of small-scale hydro-power projects. Critical advice will aim to place the bankrupt sector on a more solid financial footing primarily by encouraging residential, commercial, and industrial consumers to pay their bills on time.

Strategic Objective 2.31: “More effective, responsive, and accountable local governance” will focus on supporting the increasingly autonomous and responsive local governments. It will also support civil society, political party strengthening, media development and transparency in the management of resources and local governance institutions at the local level in the regions outside Tbilisi.

Strategic Objective 3.4: “Catalyze improvement of social and health services in targeted areas” will support sustainable development and management of social services and small-scale public works in the rural areas (mainly rehabilitation of schools, health clinics, energy sources, safe water supplies, and roads). Health programs will focus on health promotion and improvement of the efficiency of quality health care. Support will be provided for the following: reproductive health, family planning and maternal and infant care (an earmark); HIV/AIDS and tuberculosis prevention and treatment (a frequent earmark); public awareness campaigns; screening programs for early disease detection; and health care financing.

Strategic Objective 4.1: Special Initiatives (SIs) and Cross-Cutting Issues (CCIs)

1. Special Initiatives (SIs)

A. Elections Assistance: The main thrust of this activity is to support the development of a more credible and democratic electoral process. USAID will support the conduct of fair

and free Parliamentary elections in 2003 and Presidential elections in 2005. Principal activities to be supported are: political party strengthening, voter education, voter registration, and elections monitoring and observation.

B. Anti-Trafficking in Persons: In cooperation with other sections of the U.S. Embassy and with other donors, USAID will initiate a program to prevent Georgians from being trafficked for profit. A better informed public and the passage of anti-trafficking legislation will be markers of success for this activity, which is closely watched by the Department of State (DOS) and Congress alike.

C. Anti-Corruption: Corruption is a major concern in Georgia that is discouraging foreign direct investment, increasing business transaction costs, and encouraging smuggling. Corruption adversely affects the competitiveness and viability of the Georgian private sector and hurts consumers. Each SO will undertake anti-corruption activities as an integral part of its program portfolio. The funds allocated under SO 4.1's Special Initiatives are for additional analyses, assessments, small grants, and training.

2. Cross-Cutting Issues (CCIs)

A. Conflict Prevention: The conflict prevention CCI intends to reduce the risk of violence in Samtskhe-Javakheti or other similar conflict-prone regions. In coordination with USAID in Armenia and Azerbaijan, USAID/Caucasus-Georgia will continue support for the South Caucasus Regional Water Management Program (RWMP) that strives for better, long-term river basin management and increased cooperation among the three Caucasus nations.

B. Youth: Significant new efforts will develop youth as a resource for the future. The new Country Strategy will integrate civics and Junior Achievement activities. Communities will be mobilized to involve youth in local politics and to upgrade school facilities.

Strategic Objective 4.2: Program Support

These activities include the following: participant training to improve the skills of public and private sector participants directly involved in program implementation; staffing support for program management; public outreach and information; and funding for foundations. SO 4.2 also is the repository for the Program Development and Support (PD&S) funds and other administrative support accounts.

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